TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1957

No. 306

THE COLONY, INC., PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR CERTIORARI FILED JULY 22, 1957

CERTIORARI GRANTED OCTOBER 14, 1957

SUPREME COURT OF THE UNITED STATES

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INDEX

	Original	Print
Proceedings before the Tax Court of the United States	1	1
Findings of fact	3	3
Opinion, Harron, J.	17	16
Respondent's Exhibit "D"—Corporation income and declared value excess profits tax return for the fiscal year beginning November 14, 1945 and ending October 31, 1946, with attachments	30	27
Respondent's Exhibit "E"—Corporation income tax return for the fiscal year beginning November 1, 1946 and ending October 31, 1947, with attachments	39	36
Proceedings in U.S.C.A. for the Sixth Circuit	46	42
Minute entry of argument and submission (omitted in printing)	46	42
Judgment	46	42
Clerk's certificate (omitted in printing)	48	43
Order allowing certiorari	49	43

RECORD PRESS, PRINTERS, NEW YORK, N. Y., JANUARY 24, 1958

[fol. 1]

BEFORE THE TAX COURT OF THE UNITED STATES

THE COLONY, INC., Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

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26 T. C. No. 3

Docket No. 53681—Filed April 9, 1956.

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1. The petitioner is a corporation organized to acquire, subdivide, and sell real estate. It was organized with a total capital of $1,000. It obtained bank loans, secured by liens on its real estate, in an amount in excess of $149,000. Five of petitioner's stockholders paid over a total of $57,800 to petitioner and received petitioner's interest-bearing promissory notes in that amount. *Held,* the $57,800 paid over to petitioner by its stockholders constituted contributions to capital, rather than bona fide loans, and amounts paid by petitioner to the stockholders in 1948, 1949, and 1950, constituted nondeductible distributions in the nature of dividends, rather than interest on indebtedness which is deductible under section 23(b) of the 1939 Code.

2. In determining its basis for gain or loss in the subdivision lots which it sold in 1946, 1947, and 1950, the petitioner added to its cost of the lots a pro rata portion of improvement expenses which it incurred or estimated that it would incur in developing the subdivision. *Held,* the cost of a water supply system which petitioner continued to own and operate during the taxable years did not constitute a development expense which could be added to petitioner's basis in the subdivision lots; *held, further,* petitioner's basis in the subdivision lots includes the amount of payments made by petitioner to two utility companies to induce the latter to extend their services to petitioner's subdivision; *held, further,* the respondent's determination

that petitioner overestimated its development expenses in the amount of $5,550.82 is sustained.

3. For the taxable years ended October 31, 1946, and October 31, 1947, the petitioner omitted from gross income an amount properly includible therein which was in excess of 25 per cent of the gross income stated in its returns. [fol. 2] The understatements of gross income resulted from overstatements of cost of goods sold, rather than from omissions of gross receipts. *Held*, the 5-year statute of limitations contained in section 275(c) of the 1939 Code is applicable, and the deficiencies determined for the years ended October 31, 1946, and October 31, 1947, are not barred. *Estate of J. W. Gibbs, Sr.*, 21 T. C. 443, followed.

Andrew W. Duncan, Esq., and *Don S. Sturgill, Esq.*, for the petitioner.

James F. Shea, Esq., for the respondent.

The Commissioner determined deficiencies in income tax and excess-profits tax as follows:

Year ended October 31	Income Tax	Excess-Profits Tax
1946	$7,988.72	$2,356.71
1947	1,194.29	—
1948	987.31	—
1950	224.23	—

The year ended October 31, 1949, also is involved because the amount of net operating loss sustained in that year will determine the amount of net operating loss deduction allowable for the year ended October 31, 1947. The issues to be decided are (1) whether payments made by petitioner to its shareholders in the amounts of $8,988.41, $3,468, and $3,468, in the taxable years ended October 31, 1948, 1949, and 1950, respectively, were deductible by petitioner as interest payments, or whether such payments were non-deductible distributions in the nature of dividends; (2) whether petitioner's cost of subdivision lots includes the expenditures made to construct a water supply for the subdivision and the payments made to public utilities in order to induce the utilities to extend their service to the subdivision; and (3) whether the deficiencies determined

for the years ended October 31, 1946, and October 31, 1947, are barred by the statute of limitation.

[fol. 3] FINDINGS OF FACT

The petitioner is a corporation organized under the laws of the State of Kentucky. Petitioner kept its books and filed its returns on an accrual method for fiscal years ended October 31. Petitioner's returns for the taxable years were filed with the collector for the district of Kentucky.

The petitioner's principal business is the development and sale of lots in a subdivision called "The Colony," which is located outside the city limits of Lexington, Kentucky. The petitioner also owned a water supply and distribution system, and beginning in 1949, sold water to houses which were built in the subdivision.

Deduction of Payments to Stockholders

The petitioner was incorporated on or about November 14, 1945. Its authorized capital stock, which was all issued, consisted of 400 shares of capital stock without par value. Its paid-in capital was $1,000, or $2.50 per share of capital stock.

On or about April 19, 1946, Hugh Meriwether, L. J. Blakely, and Charles Sturgill, as owners of all of the petitioner's stock, entered into an agreement with Dr. Halbert Leet. The agreement recited that Dr. Leet agreed to lend petitioner, on petitioner's note, the sum of $17,500 for 5 years with interest at 6 per cent, payable semi-annually; that Meriwether, Blakely, and Sturgill agreed that they would convey to Dr. Leet, without further consideration, 10 per cent of petitioner's stock, that is, 40 shares; and that no dividends would be paid by petitioner without Dr. Leet's consent until the note was paid. The agreement between Dr. Leet and petitioner's shareholders provides, in part, as follows:

> This memorandum of agreement between Hugh Meriwether, L. J. Blakely and Charles Sturgill, of Lexington, Ky., owners of the capital stock of the Kentucky corporation The Colony, parties of the first [fol. 4] part, hereinafter called the "Stockholders," and

Dr. Halbert Leet, of Lexington, Ky., party of the second part, hereinafter called "Dr. Leet," witnesseth that it is agreed by and between the parties hereto as follows:

Dr. Leet shall lend to the said corporation, The Colony on or before the 25th day of April, 1946, the sum of Seventeen Thousand Five Hundred Dollars ($17,500.00) upon the latter's negotiable promissory note in the said sum of money to be dated the day said loan is made, and to be payable on or before five years after date, with interest thereon at the rate of 6% per annum, payable semi-annually, from its date until its payment.

The Stockholders shall, at the same time with the making of said loan, cause the said corporation to execute and deliver said note to Dr. Leet, and will assign and transfer to Dr. Leet as his own, without further consideration, ten per cent (10%) of the capital stock of said corporation: and they, and their successors, if any, in the ownership of their respective shares of stock of said corporation, shall see to it that no dividend is paid by said corporation, (except with the consent of Dr. Leet or his successors in ownership of said 10% of the stock) until said note (and any similar note issued or to be issued by the corporation under similar circumstances) shall have been paid.

On April 24, 1946, Dr. Leet paid $17,500 to petitioner in exchange for its note, and received 40 shares of petitioner's stock from Meriwether, Blakely, and Sturgill. On the same day, L. B. Shouse also paid $17,500 to petitioner in exchange for its note, and received 40 shares of petitioner's stock from Meriwether, Blakely, and Sturgill. Also, on the same day, Meriwether, Blakely, and Sturgill each paid $7,600 to petitioner in exchange for similar promissory notes. The total amount received by petitioner on April 24, 1946, from the five individuals in exchange for its notes was $57,800. The notes issued by petitioner stated that

repayment was to be made in 5 years, that is, on April 24, 1951, and that interest was payable at the rate of 6 per cent.

Prior to the end of petitioner's first fiscal year, on October 31, 1946, petitioner also issued notes in the amount of [fol. 5] $149,403 to banks. The notes held by the banks were secured by liens on petitioner's real estate.

Also, prior to October 31, 1946, Gilmore N. Nunn acquired 4 shares of petitioner's stock from Meriwether, Blakely, and Sturgill. On October 31, 1946, petitioner's stock and notes payable were held as follows:

Name	Shares of petitioner's stock	Investment in stock at $2.50 per share	Face amount of petitioner's notes
Hugh Meriwether	105⅓	$ 263.34	$ 7,600
L. J. Blakely	105⅓	263.33	7,600
Charles Sturgill	105⅓	263.33	7,600
Dr. Halbert Leet	40	100.00	17,500
L. B. Shouse	40	100.00	17,500
Gilmore N. Nunn	4	10.00	—
Total—Shareholders only	400	$1,000.00	$ 57,800
Banks	—	—	149,403
Total	400	$1,000.00	$207,203

The notes described above are reflected in the balance sheet attached to petitioner's return for the year ended October 31, 1946, as "Notes Payable-Bank Loans" in the amount of $149,403, and "Notes Payable-Stockholders" in the amount of $57,800.

None of the notes held by the stockholders has been paid by the petitioner with the exception of the note in the face amount of $17,500 issued to L. B. Shouse. At the time this note was paid, petitioner also purchased Shouse's 40 shares of stock at a price of $2.50 per share, or a total of $100. Sometime after the taxable years, in 1953, Sturgill and the Central Rock Company, a corporation, acquired the stock and notes of petitioner held by the remaining stockholders, namely, Meriwether, Blakely, Dr. Leet, and Nunn. Sturgill and the Central Rock Company now own, equally, all of

petitioner's outstanding stock, and the notes in the face amount of $40,300 which remain outstanding.

[fol. 6] In the taxable years ended October 31, 1946, and October 31, 1947, the petitioner did not pay to the holders, or accrue on its books, or claim deductions on its returns for, any amounts payable as interest on the notes held by its stockholders. In the taxable year ended October 31, 1948, the petitioner paid a total of $8,988.41 to the 5 stockholder-noteholders, and claimed a deduction in that amount in its return for interest paid. The total amount of $8,988.41 purportedly was distributed in payment of the interest due on the notes for the three years ended October 31, 1946, 1947, and 1948, as follows:

Payments for years ended October 31

Name	1946	1947	1948	Total Paid
Leet	$ 525.00	$1,081.50*	$1,114.90*	$2,721.40
Shouse	525.00	1,081.50*	1,114.90*	2,721.40
Blakely	228.00	469.68*	484.19*	1,181.87
Meriwether	228.00	469.68*	484.19*	1,181.87
Sturgill	228.00	469.68*	484.19*	1,181.87
Totals	$1,734.00	$3,572.04	$3,682.37	$8,988.41

* Six per cent interest on $17,500, the face amount of the notes held by Leet and Shouse, is $1,050 per year. Six per cent interest on $7,600, the face amount of the notes held by Blakely, Meriwether, and Sturgill, is $456.00. The difference between these amounts and the somewhat larger amounts actually paid, as set forth above, is not explained in the record.

In each of the taxable years ended October 31, 1949, and October 31, 1950, the petitioner paid $3,468 to the 5 stockholder-noteholders, and claimed deductions in that amount in its returns for each of the years for interest paid.

The respondent disallowed the entire amount claimed by petitioner as interest deductions in its returns for the taxable years ended October 31, 1948, 1949, and 1950. The deficiency notice contains the following explanation for the disallowance of the interest deduction claimed in petitioner's return for the year ended October 31, 1948:

[fol. 7] It is held that the amount of $8,988.41 deducted as interest in the return filed for the fiscal year ended October 31, 1948, constitutes dividends within the purview of Section 115 of the Internal Revenue Code, and is therefore not allowable as a deduction in computing net taxable income.

Similar explanations are given for the disallowance of the interest deductions claimed in the returns for the years ended October 31, 1949, and October 31, 1950.

Except for items representing the notes payable to stockholders and to banks, and reserve accounts for depreciation and for improvements, the following are the only liabilities set forth in the balance sheets attached to petitioner's returns for the years ended October 31, 1946, to October 31, 1950, inclusive:

	Year Ended October 31				
	1946	1947	1948	1949	1950
Accounts Payable	$ 165.65	—	—	—	—
Accrued Taxes	5,160.09	$1,000.43	$4,033.84	$986.94	$1,004.48
Total	$5,325.74	$1,000.43	$4,033.84	$986.94	$1,004.48

The $57,800 paid to petitioner by the 5 shareholders in 1946 in return for petitioner's promissory notes constituted contributions to petitioner's capital rather than bona fide loans. The payments in the fiscal years ended October 31, 1948, 1949, and 1950, to the 5 stockholder-noteholders in the amounts of $8,988.41, $3,468, and $3,468, respectively did not represent payments of interest.

Cost of Subdivision Lots to Petitioner

Issue 2: Shortly after its organization, petitioner acquired a farm near Lexington, Kentucky. The farm was approximately 228 acres in size, and was acquired by petitioner for the purpose of subdivision into residential lots. The petitioner's plan of operation was to sell lots to indi-

vidual buyers, rather than to construct and sell homes. The petitioner sold lots in each of the years ended October 31, 1946, 1947, and 1950.

[fol. 8] For the purposes of reporting gain from the sale of lots, petitioner included as part of its cost or other basis in the lots a proportionate part of the estimated cost of developing the subdivision. The amount of estimated development expenses added by petitioner to its cost of the lots was $93,074.61, and the total basis claimed by petitioner in the subdivision amounted to $131,550. As is more fully set forth hereinafter, the respondent determined that the amount of development costs which were includible in the computation of petitioner's cost or other basis in the lots did not exceed $44,988.55, and that petitioner's total basis in the subdivision did not exceed $83,463.94. The amount of development expenses claimed by petitioner which was disallowed by respondent, $48,086.06, represents the following three items: The portion of the original estimated cost of development, $93,074.61, which petitioner had not expended as of September 30, 1950; the expenditures made by petitioner to acquire a water supply system; and the amount of payments made by petitioner to two utility companies. The amount of each of the three items is as follows:

Unexpended part of estimated development costs	$ 5,590.82
Expenditures for water supply system	33,781.70
Payments to utility companies	8,713.54
Total	$48,086.06

The first part of petitioner's real estate to be subdivided was The Colony, which comprised about 65 lots covering approximately 60 acres. When subdivision of The Colony began, there was no available source of water. Without water, the lots would not have been saleable. The petitioner was advised that it would cost between $40,000 to $60,000, and perhaps more, to connect The Colony with the facilities of the Lexington Water Company, which were approximately 1½ miles away. The petitioner's stockholders decided that petitioner would construct a water system to provide water to lot purchasers instead of entering into any

arrangement with the Lexington Water Company. Prior [fol. 9] to 1949, the petitioner completed a water supply and distribution system for The Colony. The chief source of water for the system is a well capable of producing 576,000 gallons of water each 24 hours. Water from the well is pumped automatically by turbine pump through a chlorination tank to a 55,000-gallon capacity concrete pool, and then, by highlift pumps, into a 3,000-gallon capacity steel pneumatic tank. For convenience, the portion of the water system described above is referred to as the "pumping system." From the pneumatic tank, the water passes into the "distribution system," which consists of 6,500 feet of 4- and 6-inch pipe, about 2,500 feet of 2-inch pipe, and meters to the various houses.

In a brochure put out by petitioner, the water system is described as follows:

> In order to provide fire protection and to supply home owners in The Colony, with pure, soft water, The Colony will have its own private water works. The chief source is a well which is now producing 576,000 gallons of pure water each twenty-four hours, sufficient for the normal use of 14,000 people. Water will be supplied to home owners from a 55,000-gallon concrete reservoir. The water supply will at all times be under the supervision of the State and County Boards of Health.

The water system constructed by the petitioner was intended to supply 20 houses to be located near The Colony, as well as the houses located in The Colony subdivision. Also, during the taxable year ended October 31, 1948, the petitioner sold an additional 40 acres of land from the original farm tract. The 40 acres were sold at public auction, and in order to induce purchasers to pay a higher price, the petitioner agreed to provide water for the land.

The total cost incurred by petitioner in constructing the water supply system was $33,781.70, as follows:

[fol. 10]	Pumping System	$16,528.12
	Distribution System	13,885.31
	Engineering fees	2,864.18
	Unclassified	504.09
	Total	$33,781.70

The petitioner retained easements over lots which it sold in The Colony. These easements reserved to petitioner the right to maintain its water distribution system on the lots, but did not obligate petitioner to do so.

The water supply system began operation sometime during the taxable year ended October 31, 1949. Water meters installed by petitioner measured the water supplied to the houses served by the water distribution system, and petitioner was paid by the consumers for the water it provided. In the taxable years ended October 31, 1949, to October 31, 1954, inclusive, petitioner realized, from the operation of its water supply system, the following amounts of gross receipts and profit or loss, the profit or loss being computed without deductions for electricity expense or depreciation:

Year ended October 31	Gross receipts	Net profit (or loss) before deduction for electricity or depreciation
1949	$211.89	$(249.71)
1950	583.12	155.99
1951	258.08	(182.12)
1952	350.38	(382.39)
1953	421.37	(260.61)
1954	408.59	(183.96)

The largest item of expense incurred by the petitioner in the operation of the water system was for wages. L. J. Blakely, who lived near the pump site, was paid $300 per year to "look after" the water system in the years ending October 31, 1949, 1950, and 1951; $440 in the year ended October 31, 1952; $480 in the year ended October 31, 1953; and $400 in the year ended October 31, 1954.

[fol. 11] The number of houses to which petitioner supplied water in each of the years set forth above is not shown in the record before us.

Throughout the taxable years and thereafter, the petitioner retained full ownership and control of the assets comprising the water supply system.

In 1948 and 1949, petitioner made payments to the Kentucky Utilities Company (hereinafter called Utilities Company) and the Central Kentucky Natural Gas Company (hereinafter called Gas Company), pursuant to agreements between petitioner and the companies relating to the exten-

sion of gas and electricity service to The Colony. Petitioner's contract with the Gas Company was dated October 16, 1946. Petitioner entered into two contracts with the Utilities Company, one dated December 17, 1947, and the other dated December 1, 1949. The total payments made by petitioner to the two companies under the contracts amounted to $8,713.54, as follows:

Payee	Date of Payment	Amount of Payment
Gas Company	January 6, 1948	$6,535.00
Utilities Co.	March 19, 1948	1,427.93
" "	December 17, 1949	750.61
	Total	$8,713.54

The payments made by petitioner were required by the companies before the latter would extend their services to The Colony. The contracts between petitioner and the companies provided that all or a part of the payments might be refunded to petitioner. For example, the contract with the Gas Company provided that the latter would refund to petitioner a total of $75 for each new customer connected to the company's gas mains, but that no refund would be made after 10 years from date of the contract, that is, after October 16, 1956. Each of the contracts with the Utilities Company provided for the refund of approximately $160 to petitioner for each new customer connected to the company's electric line, but that no refund would be made after 5 years from the time of completion of the service extensions pro-
[fol. 12] vided for in the contracts. Exhibits 16 and 17 are incorporated by this reference. Up to the date of the hearing of this proceeding, the petitioner had received refunds of $1,407.41 from the Utilities Company and $750 from the Gas Company, or a total of $2,157.41, as follows:

Date of Refund	Refunds from Utilities Co.	Refunds from Gas Co.
Nov. 9, 1948	$162.27	$150
May 23, 1949	162.27	—
May 28, 1949	—	150
1951	491.49	450
1954	591.38	—
Totals	$1,407.41	$750

An account titled "Reserve for Improvements" was set up on petitioner's books and credited on September 30, 1946, in the amount of $93,074.61. This amount represented petitioner's estimate of the costs which would be incurred in the development of The Colony, and petitioner added a pro rata portion of this amount to its cost of each of the lots which it sold in the taxable years ended October 31, 1946, 1947, and 1950.

The reserve account was debited in the amount of each expenditure which petitioner considered an expense of development for the subdivision. As of September 30, 1950, the total amount debited to the reserve account was $87,-483.79, and on that date there remained, from the original credit entry of $93,074.61, a credit balance of $5,590.82. The total amount debited to the reserve account, $87,483.79, consisted of the following entries: $33,781.70, the cost of the water supply system; $8,713.54, the total of the payments made to the utility companies; and $44,988.55 for other expenditures which are not in issue.

For the purpose of computing gain from the sale of the lots which were sold in 1946, 1947, and 1950, the petitioner added a proportionate part of $93,074.61, the amount originally credited to the reserve account for improvements to its cost of the lots sold. In its returns for the years ending [fol. 13] October 31, 1946, 1947, and 1950, petitioner reported gain from the sale of lots and gross income, as follows:

	Year ended October 31		
	1946	1947	1950
Selling Price of Lots	$78,987.50	$28,075.00	$8,000.00
Less Cost of Lots Sold	57,375.00	18,575.00	7,500.00
Gross profit on sale of lots	$21,612.50	$ 9,500.00	$ 500.00
Other income	637.53	8,595.41	8,909.25
Gross income reported	$22,250.03	$18,095.41	$9,409.25

The respondent determined that the development costs which might be added to petitioner's cost of the lots did not exceed $44,988.55. Accordingly, the respondent determined that petitioner had overstated its cost of the lots in

the total amount of $48,086.06, which is the difference between the estimated development costs claimed by petitioner, $93,074.61, and $44,988.55, the amount determined by respondent. The respondent also determined that petitioner overstated the costs of lots sold and understated the profit from lot sales in the years ended October 31, 1946, 1947, and 1950, in the amounts of $20,972.54, $6,789.80, and $2,741.51, respectively. The amount of the adjustment in each of these years is the portion of the total overstatement of cost determined by respondent, $48,086.06, which is allocable to the lots sold in each year. The method used by respondent to redetermine petitioner's cost of the lots sold in each year is as follows: The petitioner claimed a basis of $131,550 in the entire subdivision, after adding in the amount of $93,074.61 for the estimated cost of improvements. The respondent determined that petitioner overstated its basis in the amount of $48,086.06, and that the petitioner's basis did not exceed $83,463.94. The basis determined by respondent, $83,463.94, amounted to 63.44655 per cent of the basis reported by petitioner. Accordingly, respondent allowed petitioner, as the cost of the lots it sold each year, an amount equal to 63.44655 per cent of the cost claimed by petitioner in its returns.

[fol. 14] The deficiency notice contains the following explanation for respondent's determination that petitioner realized additional income in the amount of $20,972.54 from the sale of lots in the year ended October 31, 1946:

> It is held that the cost of lots sold in the fiscal year ended October 31, 1946, reported in the return filed for that year as amounting to $57,375.00, is not in excess of the amount of $36,402.46, the reduction representing the allocable portion of the following items incorrectly included in the computation of the total cost of the lots in the subdivision (Sections 24(a)(2) and 43 of the Internal Revenue Code):

(a) Cost of water system	$33,781.70
(b) Deposits with utility companies	8,713.54
(c) Excessive provision, reserve for improvements	5,590.82
	$48,086.06

Similar explanations appear for the adjustments determined by respondent for the years ended October 31, 1947, and October 31, 1950.

The total amount of development costs includible in petitioner's basis in the subdivision lots is $53,702.09. This amount is the total of the development expenses incurred by petitioner which are not in issue, $44,988.55, and the total of the payments made by petitioner to the utility companies, $8,713.54. The estimated development costs claimed by petitioner, $93,074.61, were overstated in the total amount of $39,372.52. The basis in the subdivision lots claimed by petitioner, $131,550, also was overstated in the total amount of $39,372.52. Petitioner's basis in the subdivision lots did not exceed $92,177.48, or 70.07 per cent of the basis it claimed.

Petitioner's basis for gain in the lots it sold in the years ended October 31, 1946, 1947, and 1950, did not exceed 70.07 per cent of the basis claimed in its returns for each of these years. Petitioner's basis in the lots sold in these 3 years were $40,202.66, $13,015.50, and $5,255.25, respectively, computed as follows:
[fol. 15]

Year ended October 31	Basis per return	70.07 per cent of basis reported in return
1946	$57,375	$40,202.66
1947	18,575	13,015.50
1950	7,500	5,255.25

Statute of Limitations

Issue 3: In the taxable years ended October 31, 1946, and October 31, 1947, petitioner's gross income amounted to $39,422.37 and $23,654.91, respectively, computed as follows:

	Year ended October 31	
	1946	1947
Selling price of lots (per return)	$78,987.50	$28,075.00
Basis in lots	40,202.66	13,015.50
Profit from sale of lots	$38,784.84	$15,059.50
Other income (per return)	637.53	8,595.41
Total	$39,422.37	$23,654.91

In each of the years ended October 31, 1946, and October 31, 1947, petitioner omitted from gross income an amount properly includible therein which was in excess of 25 per cent of the amount of gross income stated in its returns. The following schedule sets forth, for the years ended October 31, 1946, and October 31, 1947, the amount of petitioner's gross income; the amount of gross income reported by petitioner; the amount of gross income omitted from petitioner's returns; and the percentage which the gross income omitted bears to the gross income reported:

	Year ended October 31	
	1946	1947
Gross income	$39,427.37	$23,654.91
Gross income reported	22,250.03	18,095.41
Gross income omitted	$17,172.34	$ 5,559.50
Gross income omitted as percentage of gross income reported	77.2%	30.7%

[fol. 16] Petitioner's income and declared value excess-profits tax return for the taxable year ended October 31, 1946, was filed on January 15, 1947. More than 3 years and less than 5 years later, on October 17, 1951, petitioner executed an agreement under the provisions of section 276(b) of the 1939 Code extending the period of limitations for the assessment and collection of deficiencies for the year ended October 31, 1946, to June 30, 1952. On May 14, 1952, petitioner executed a second agreement extending the period to June 30, 1953; and on April 25, 1953, petitioner executed a third agreement extending the period to June 30, 1954.

Petitioner's return for the taxable year ended October 31, 1947, was filed on December 22, 1947. More than 3 years and less than 5 years later, on May 14, 1952, petitioner executed an agreement under the provisions of section 276(b) of the Code extending the period of limitation to June 30, 1953. On April 25, 1953, petitioner executed a second agreement extending the period to June 30, 1954.

The respondent's statutory notice of deficiency for the years ended October 31, 1946, and October 31, 1947, was mailed on March 29, 1954.

[fol. 17] OPINION

HARRON, *Judge: Issue 1:* The first question to be decided is whether the payments made by petitioner to five of its stockholders in the amounts of $8,988.41, $3,468, and $3,468, in the taxable years ended October 31, 1948, 1949, and 1950, respectively, were payments of interest on indebtedness, which are deductible under section 23(b) of the 1939 Code, or whether the payments constituted nondeductible distributions in the nature of dividends. The determination of this issue depends on whether the $57,800 paid by the shareholders to petitioner in return for petitioner's notes constituted, in substance, a loan giving rise to a creditor-debtor relationship, or a contribution to capital, which gave the stockholders an additional proprietary interest.

The petitioner concedes that it is a "thin corporation." It argues, however, that the notes must be recognized as a valid indebtedness because the petitioner's capitalization reflected the business judgment of unrelated persons who dealt with each other at arm's length; because the notes were issued to the stockholders in face amounts which were disproportionate to their stock holdings; and because the transaction was carried out in the form proper to create an indebtedness, rather than a contribution to capital. The respondent takes the position that the $57,800 paid in by the shareholders must be considered as a contribution on their part to petitioner's capital, in view of the capital structure of the petitioner; the circumstances under which the notes were issued, and the lack of evidence indicating that the transaction was intended to create a debtor-creditor relationship.

The question to be decided is one of fact. *Sam Schnitzer,* 13 T.C. 43, 60, affd. 183 F.2d 70, certiorari denied 340 U.S. [fol. 18] 911. The issue is whether there was an intention to create a debtor-creditor relationship, on the one hand, or a capital contribution, on the other hand, "and such intention is a fact to be gleaned from the entire record." *Estate of Herbert B. Miller,* 24 T.C. 923. It is true, in this case, that the notes received by the 5 shareholders upon their payment of $57,800 to petitioner satisfy the formal requirements for a corporate indebtedness. However, our inquiry is not limited to the formalities, however meticu-

lously observed, in which the parties cast their transaction. *R. M. Gunn*, 25 T.C. —— (December 9, 1955); *Estate of Herbert B. Miller, supra; Gooding Amusement Co.*, 23 T.C. 408, 418; *Proctor Shop, Inc.*, 30 B.T.A. 721, affd. 82 F.2d 792. There are other factors present which establish that the $57,800 was paid over to petitioner by the stockholders to be placed immediately at the risk of petitioner's business as a capital contribution rather than as a true loan.

In the first place, the petitioner's formal capital, $1,000, was patently inadequate to carry on the business for which it was formed. The petitioner was organized to purchase, subdivide, and sell a substantial tract of land. For this purpose, petitioner's formal capital of $1,000 was wholly insignificant. To finance the project, the additional amount of $57,800 was turned over to petitioner by the stockholders, and in addition the petitioner obtained loans of at least $149,403 from banks. The bank loans were secured by liens on petitioner's real estate. The notes received by the stockholders were not secured. If petitioner's characterization of the transaction is accepted, it is apparent that petitioner's business was placed in operation with loans in the amount of $207,203, and formal capital in the amount of $1,000. This alleged arrangement, which amounts to an indebted- [fol. 19] ness to capital ratio of greater than 207-to-1, clearly establishes that petitioner was undercapitalized and strongly suggests that the shareholders recognized that the $57,800 would be risked in petitioner's business as a capital contribution to the same extent as the formal capital of $1,000. See *Hilbert L. Bair*, 16 T.C. 90, affd. 199 F.2d 589. In these circumstances, we think our language in *Isidor Dobkin*, 15 T.C. 31, 33, affd. 192 F.2d 392, is particularly appropriate:

> When the organizers of a new enterprise arbitrarily designate as loans the major portion of the funds they lay out in order to get the business established and under way, a strong inference arises that the entire amount paid in is a contribution to the corporation's capital and is placed at risk in the business. *Cohen* v. *Commissioner*, 148 F.2d 336; *Joseph B. Thomas*, 2 T.C. 193. The formal characterization as loans on the part of the controlling stockholders may be a relevant factor

but it should not be permitted to obscure the true substance of the transaction. *Sam Schnitzer*, 13 T.C. 43, 60.

The conclusion that the parties did not regard the payment of the $57,800 to petitioner as a loan is also supported by their conduct subsequent to the issuance of the notes in April 1946. For example, the notes were not paid on the due date, namely, 5 years after issue, i.e., in April 1951. In fact, the evidence indicates that only one of the notes, that issued to L. B. Shouse, has been retired, and that the other notes were still outstanding at the time of the hearing of this proceeding. The stockholders other than Shouse held their notes as late as 1953, 2 years after the due date, and the evidence does not indicate that any attempt to enforce payment was ever made at any time after the due date. The parties treated their shares of stock and the notes as part of a single package whenever a transfer was made. For example, when petitioner acquired Shouse's note, it also acquired his stock. Similarly, in the transaction in 1953, in which Sturgill and Central Rock Company acquired, in [fol. 20] equal shares, the outstanding stock of petitioner held by Meriwether, Blakely, Leet, and Nunn, the notes held by the latter four persons also were acquired.

On the basis of the foregoing, it is concluded that the petitioner has failed to establish that the notes issued to its shareholders in the face amount of $57,800 represented a valid indebtedness. It is held that the respondent properly disallowed the deductions claimed by petitioner for interest on indebtedness for the years ended October 31, 1948, 1949, and 1950, in the respective amounts of $8,988.41, $3,468, and $3,468.

In reaching our conclusion we have considered petitioner's contentions concerning the disproportionate holdings among the shareholders of stock and notes. Under the circumstances of this case, we attribute to this no greater weight than if petitioner had issued disproportionate amounts of common and preferred stock. Similarly, we consider of little weight petitioner's argument that the obligations represented by the notes were not subordinated to claims of other creditors. It is true that the notes, on their

face, were not subordinate obligations. Under the facts of this case, however, little significance can be attached to this factor. For one thing, there was a lien on petitioner's principal asset, its real estate, in favor of the banks. This lien secured loans made by the banks to petitioner in the original amount of at least $149,403. In the second place, it appears that petitioner's liabilities in each of the taxable years were in negligible amounts, compared to the $57,800 in question. For example, petitioner's liabilities at the end of the taxable years October 31, 1946, to October 31, 1950, ranged from a low of $986.04 on October 31, 1949, to a high of $5,325.74 on October 31, 1946, and averaged $2,470.29. On the entire record, it is concluded that the respondent must be sustained on this issue.

[fol. 21] *Cost of Subdivision Lots to Petitioner*

Issue 2: The narrow question to be decided under this issue is the proper amount which petitioner may add to its cost of Colony lots for the cost of development work in The Colony subdivision. It is well established that where subdivision lots are sold before development work is completed, the seller may include in his cost of the lots an allocation of his estimated future expenditures for improvements to the subdivision. *Country Club Estates, Inc.*, 22 T.C. 1283, 1293-1294; *Cambria Development Company*, 34 B.T.A. 1155.

The petitioner included in its cost of Colony subdivision lots a total of $93,074.12 for development expenses, and added a pro rata portion of this total to its cost of The Colony lots which it sold in the taxable years ended October 31, 1946, 1947, and 1950. The respondent determined that the development expenses claimed by petitioner were excessive, and that the proper amount to be added to petitioner's cost of the lots did not exceed $44,988.55. The respondent accordingly reduced the cost or other basis which the petitioner claimed in the lots which were sold, and increased the profit reported by petitioner from the sale of these lots. The amount by which the respondent reduced the petitioner's cost or other basis in the lots in each of the years ended October 31, 1946, 1947, and 1950, equaled a pro rata part of $48,086.06, the total amount by which the respondent reduced the development costs claimed by petitioner. The

petitioner does not contest the percentage method used by respondent to redetermine the cost of the lots, in the event it is determined that petitioner overstated its development costs. The petitioner does claim, however, that its development costs were not overstated in the amount determined by the respondent.

[fol. 22] The amount of estimated development costs disallowed by respondent, $48,086.06, is the total of three items, namely, an expenditure of $33,781.70 to construct a water supply system; payments to utility companies in the amount of $8,713.54; and the sum of $5,590.82, which is the excess of the petitioner's estimated development costs of $93,074.61 over the total amount it claimed to have expended for development purposes as of September 30, 1950, namely, $87,483.79. The respondent, in effect, allowed as development costs the total amount petitioner claimed to have expended as of September 30, 1950, other than the cost of the water supply system and the amounts paid to utility companies.

The respondent's position under this issue is that the expenditures incurred to acquire the water supply system and to make payments to the utility companies are not properly chargeable to development costs which can be added to the cost of the subdivision lots. In the case of the portion of the estimated costs which petitioner had not expended as of September 30, 1950, or $5,590.82, the respondent contends that no part of the $5,590.82 will be required for future improvements, and that petitioner's original estimate of $93,074.61 for future developments was excessive in the amount of $5,590.82. The three adjustments will be discussed separately.

Petitioner introduced no evidence at the hearing of this proceeding to establish that further development work was required at The Colony after September 30, 1950, or that any expenditures were in fact made after that date for purposes of development or improvement. We accordingly sustain respondent's determination that the petitioner's estimate for future development costs, $93,074.61, was excessive in the amount of $5,590.82, which is the portion of petitioner's estimate which had not been expended as of September 30, 1950. *Butler-Fornari Realty Corporation*, 37 B.T.A. 933.

[fol. 23] The next item under this issue relates to the water supply system. The petitioner has abandoned its original contention that the entire cost of the water supply system is a development expense which can be allocated to its cost of the subdivision lots. It concedes now that the "distribution system" or piping which carried the water from the "pumping system" to the houses, is not a development expense. It now claims that only the cost of the pumping station or pumping system is a development cost which should be added to its cost of the lots. The petitioner contends that the lots were unsaleable without a water supply system, and that it was required to construct such a system because the cost of connecting the subdivision with the facilities of the Lexington Water Company was prohibitive. The petitioner contends further that when the facilities of the Lexington Water Company eventually extend to the subdivision, the pumping station will be of no further use and will have no value other than for salvage. The petitioner contends that under these facts, the cost of the pumping system must be added to its cost of the lots. The petitioner relies on *Country Club Estates, Inc., supra*. In that case, the taxpayer was in the business of selling subdivision lots. In order to induce people to purchase lots, the taxpayer conveyed a portion of its tract to a nonprofit organization for the purpose of having a country club constructed. It was held that the cost of the property transferred by the taxpayer should be regarded as part of its basis in the subdivision lots which it sold.

The difficulty with petitioner's contention is that, unlike the taxpayer in *Country Club Estates, Inc., supra*, the petitioner has not given up any property in order to sell its lots. For the funds it expended, the petitioner acquired a water supply system which it owned and operated during [fol. 24] the taxable years and thereafter. It is true that the system has not been operated at a profit, due, perhaps, to the small number of houses which have been constructed at The Colony. And it also may be true, as petitioner contends, that the pumping station may be abandoned at some time in the future, when the facilities of the Lexington Water Company reach the subdivision. These circumstances, however, do not alter the fact that the petitioner

retained full ownership and control of the water supply system during the taxable years, and that it did not part with the property for the benefit of the subdivision lots. Because of this retention of ownership, *Country Club Estates, Inc., supra,* is distinguishable. The retention of ownership also distinguishes this proceeding from cases in which the subdivider is permitted to add to his cost of lots the cost of land which has been dedicated or donated for use as streets. See, *Commissioner* v. *Laguna Land & Water Co.*, 118 F.2d 112, modifying, on other grounds, a Memorandum Opinion of the Board of Tax Appeals. We think the facts in this proceeding more closely resemble *Biscayne Bay Islands Co.*, 23 B.T.A. 731. In the latter case, the taxpayer subdivided for sale the waterfront portion of its property. The interior portion of its property was set aside, for a term of years only, and not irrevocably, for use as a public park. It was held that the taxpayer's cost of the waterfront lots did not include the cost of the interior park property because the taxpayer had not irrevocably parted with the interior property. We said (page 735):

> * * * This area was not permanently and irrevocably dedicated to the public, but may later be sold by petitioner. The possibility of gain has only been postponed. It is unlike the area used for public streets, which is permanently beyond the possibility of sale and gain, the cost of which must be absorbed in the salable lots. See *Oak Woods Cemetery Association,* 6 B.T.A. 1003.

[fol. 25] It is held that the cost of the water supply system may not be added to the cost of The Colony subdivision lots for the purposes of computing petitioner's gain on the sale of such lots.

There is an additional dispute between the parties which relates to the cost of the water supply system. The respondent determined that the total cost of the system which the petitioner had added to its cost of the lots was $33,781.70. The petitioner claims that the cost of the system was $33,277.61, or $504.09 less than the amount determined by respondent. The question is one of fact and the petitioner has the burden of proving the respondent's determination erroneous. The cost of the water supply system was not

separately stated in the books of account maintained by petitioner. Petitioner relies, in support of its contention, on an analysis of invoices made by the engineer who supervised the construction of the water supply system. However, the evidence indicates that the engineer did not have available all the invoices relating to the construction of the system. At one point the engineer testified that "practically all" the bills for materials and services came into his hands; elsewhere, he stated that the bills of which he had knowledge accounted for about 80 per cent of the cost of the project. In either event, the petitioner has not established that the engineer upon whose testimony it relies had knowledge of the total cost of the system. It is concluded that the petitioner has failed to establish that the cost of the water supply system was less than the amount determined by the respondent. It is held that the cost of the water supply system was $33,781.70, and that this amount is not includible in the cost of The Colony lots sold by petitioner.

The final question relating to the petitioner's cost of The Colony lots concerns the payments made by petitioner to the Gas Company and to Utilities Company. The petitioner [fol. 26] made payments to the companies in the total amount of $8,713.54, and included this amount in the cost of its Colony lots. The respondent takes the position that the petitioner is not entitled to add any part of the payments to the cost of the lots it sold during the taxable years, because there existed a possibility that all or a part of the payments might be refunded to petitioner at some time after the taxable years.

The evidence establishes that the companies required the payments to be made before they would extend their services to Colony. The payments were made to the companies in accordance with written agreements, the pertinent provisions of which are stated in the findings. Pursuant to the contract with the Gas Company, the petitioner paid $6,535 to the Gas Company in January 1948. The contract provided that the petitioner would receive a refund of $75 for each new customer connected to the company's gas mains, but that no refund would be made after 10 years from the date of the contract, i.e., after October 16, 1956. In the case of the second compa[redacted], the Utilities Company,

the petitioner made payments in the total amount of $2,178.54 in 1948 and 1949. The contracts with the Utilities Company provided that a refund of approximately $160 would be paid to petitioner for each new customer connected to the company's electric line, but that no refund would be made after 5 years from the time of completion of the service extensions provided in the contract. The period during which petitioner was entitled to receive refunds from the Utilities Company did not expire during the taxable years.

It is true, therefore, as respondent contends, that there was no way to ascertain, during the taxable years, the total amount of refunds which petitioner might receive under its [fol. 27] contracts with the two companies. We do not think, however, that this circumstance militates against the petitioner. The determinative factor is that the petitioner made unconditional payments to the two companies in order to obtain utility service for The Colony, and thereby to attract customers for The Colony lots. The payments were thus closely related to the sale of the lots, and petitioner's income from the sale of lots will be more clearly reflected if a pro rata portion of the payments in question are included in its basis for gain or loss in each lot which was sold. On the other hand, the receipt of refund payments from the utility companies is less closely related to the improvement of the lots for sale. The payment of a refund would be made only if a new customer was connected to the utility companies' service extensions, rather than at the time a lot was sold. Thus, if lots were sold to purchasers who, for some reason, did not proceed to construct residences, the petitioner would not receive refunds; or, if a purchaser acquired two or more lots, on which only one residence was constructed, the petitioner would receive only one refund, rather than a number of refund payments equal to the number of lots sold to the purchaser. Under these circumstances, it is concluded that the payments to the utility companies were directly related to the improvement of The Colony lots for sale, and that the petitioner correctly included these payments in computing its basis for gain or loss in the lots which it sold. The question of the taxability of the refunds which petitioner may receive from the utility companies is not before

us. It is noted, however, that the petitioner concedes, on brief, that such refunds would, if made, constitute taxable income. See, *Chevy Chase Land Co.*, 34 B.T.A. 150.

Issue 3: The final question to be decided is whether the deficiencies determined for the taxable years ending October 31, 1946, and October 31, 1947, are barred by the statute of limitations. The deficiency notices for these 2 years [fol. 28] were mailed within the extended period provided in waivers which the petitioner originally executed more than 3 years and less than 5 years after the returns were filed. The question is whether the 5-year statute of limitations contained in section 275(c) of the 1939 Code[1] is applicable in this proceeding. The petitioner omitted from gross income in each year an amount properly includible therein which was in excess of 25 per cent of the gross income reported. The petitioner contends, however, that section 275 (c) is inapplicable because the omission resulted from an overstatement of cost of goods sold, rather than from an omission of gross receipts. The petitioner relies on *Uptegrove Lumber Co.* v. *Commissioner*, 204 F.2d 570, reversing a Memorandum Opinion of this Court, and on *Deakman-Wells Co., Inc.* v. *Commissioner*, 213 F.2d 894, reversing 20 T.C. 610. Our holding in *Estate of J. W. Gibbs, Sr.*, 21 T.C. 443, however, requires that this issue be decided in favor of the respondent. We have recently reviewed the decision in the *Gibbs* case in the light of the decisions in the *Uptegrove Lumber Co.* and *Deakman-Wells Co., Inc.* cases, and have decided to adhere to the rule in the *Gibbs* case. *John E. Goodenow*, 25 T.C. —— (October 6, 1955). On the basis

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[1] SEC. 275. PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION.

Except as provided in section 276—

* * * * * * *

(c) Omission From Gross Income.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

of the *Gibbs* and *Goodenow* cases, it is held that the 5-year statute of limitations in section 275(c) is applicable, and that the deficiencies determined for the years ending October 31, 1946, and October 31, 1947, are not barred by the statute of limitations.

Decision will be entered under Rule 50.

[fol. 30]

Computation proved

Fiscal Year

Form 120

Treasury Department
Internal Revenue Service

UNITED STATES
CORPORATION INCOME AND DECLARED VALUE EXCESS-PROFITS TAX RETURN 1945

THE TAX COURT OF THE U.S. DIV. 13 DECEMBER ... ADMITTED ... OCT 26 1955 PETITIONER'S EXHIBIT RESP...

For Calendar Year 1945

or fiscal year beginning Nov. 14, 1945, and ending Oct. 31, 1946

PRINT PLAINLY CORPORATION'S NAME AND ADDRESS

The Colony (Name)

c/o Charlie Sturgill Motor Co. (Street and number)

Lexington (City or town, postal zone number) Kentucky (State)

NOT INVESTIGATED

Kind of business: Farm - Subdivision

Business group serial number (from Instruction N) ..... Number of places of business .....

File Code 1947 10
Serial No. 111
District Kentucky
(Number) (street)
FAY...
JAN 1947
L...
C... Church M. O.
First Payment
$ 1617 11

RECD WITH LETTER DATED JA. 15 1947 COLL. INT. DIST. OF KY.

Item and Instruction No.			
	GROSS INCOME		
1.	Gross sales (where inventories are an income-determining factor) $; Less: Returns and allowances $		
2.	Less: Cost of goods sold. (From Schedule A)		
3.	Gross profit from sales		
4.	Gross receipts (where inventories are not an income-determining factor) $		
5.	Less: Cost of operations. (From Schedule B)		
6.	Gross profit where inventories are not an income-determining factor		
7.	Interest on loans, notes, mortgages, bonds, bank deposits, etc.		
8.	Interest on corporation bonds, etc. $ Less Amortizable Bond Premium $		
9.	(a) Interest on United States savings bonds and Treasury bonds owned in excess of the principal amount of $5,000 issued prior to March 1, 1941. (From Schedule M, line 18 (a) (2) (iii))		
	(b) Interest on Treasury notes issued on or after December 1, 1940, and obligations issued on or after March 1, 1941, by the United States or any agency or instrumentality thereof. (Submit schedule)		
10.	Rents		
11.	Royalties		
12.	(a) Excess of net short-term capital gain over net long-term capital loss. (From Schedule C)		
	(b) Net gain (or loss) from sale or exchange of property other than capital assets. (From Schedule D)		
13.	Dividends. (From Schedule E)		
14.	Other income. (State nature)		
15.	Total income in items 3, and 6 to 14, inclusive		$ 22,250 03
	DEDUCTIONS		
16.	Compensation of officers. (From Schedule F)	$	
17.	Salaries and wages (not deducted elsewhere)		
18.	Rent		
19.	Repairs		
20.	Bad debts (From Schedule G)		
21.	Interest		
22.	Taxes. (From Schedule H) (Deduct declared value excess-profits tax as item 35)		
23.	Contributions or gifts paid. (From Schedule I)		
24.	Losses by fire, storm, shipwreck, or other casualty, or theft. (Submit schedule)		
25.	Depreciation. (From Schedule J)		
26.	Depletion of mines, oil and gas wells, timber, etc. (Submit schedule)		
27.	Net operating loss deduction. (Submit statement)		

Schedule

91

27

[fol. 31]

computation proved

Form 1121
Treasury Department
Internal Revenue Service

Fiscal Year

UNITED STATES
CORPORATION EXCESS PROFITS TAX RETURN
For Calendar Year 1945

Page 1

1945

or fiscal year beginning Nov. 14, 1945, and ending Oct. 31, 1946

PRINT PLAINLY CORPORATION'S NAME AND ADDRESS

The Colony
(Name)
c/o Charlie Sturgill Motor Co.,
(Street and number)
Lexington, Kentucky
(City or town, postal zone number) (State)

Business group serial number entered on page 1, Form 1120

File Code
Serial No.
District

EXCESS PROFITS TAX COMPUTATION

	Column 1 Income Credit Method	Column 2 Invested Capital Credit Method
1. Excess profits net income (line 18, Schedule A)		$ 18,313 00
2. Specific exemption		$ 10,000 00
3. Excess profits credit—based on income (line 40, Schedule B)		x x x x x x x x x x
4. Excess profits credit—based on invested capital (line 40, Schedule C)	x x x x x x x x x x	$ 3,228 29
5. Unused excess profits credit adjustment (attach schedule)		
6. Total of items 2 to 5		$ 13,228 29
7. Difference between item 1 and item 6		$ 5,084 71
8. Adjusted excess profits net income (item 7, column 1, or item 7, column 2, whichever is applicable)		$ 5,084 71
9. 95 percent of item 8		$ 4,830 47
10. Net income (item 30, page 1, Form 1120)		$
11. Less: (a) Dividends received credit (85 percent of total of column 2, Schedule F, Form 1120, but not in excess of 85 percent of item 10 above (excluding from the computation dividends received on certain preferred stock of a public utility))	$	
(b) Credit for dividends paid on certain preferred stocks if taxpayer is a public utility (20 percent of line 20, page 2, Form 1120)		
12. Surtax net income (computed without regard to the credit provided in section 26 (e) (sum of lines 18 and 21, page 2, Form 1120) and without regard to 80 percent of the credit provided in section 26 (h))		$
13. 80 percent of item 12		
14. Income tax under Chapter 1 (other than section 102) for the taxable year (item 42, page 1, Form 1120)		
15. Excess of item 13 over item 14		$
16. Item 9, or item 15, whichever is lesser		$
17. Amount deferred by reason of the application of section 710 (a) (5) (relating to abnormality under section 722) (attach schedule)		$
18. Excess profits tax:		
(a) Item 16 minus item 17	$	
(b) If schedule is filed under question (g), page 2, amount of tax as computed in such schedule		
(c) Item 18 (a) or item 18 (b), whichever is applicable		$
19. Less: Credit for income taxes paid to a foreign country or United States possession allowed to a domestic corporation (portion not used in computing item 43, page 1, Form 1120)		
20. Item 18 (c) minus item 19		$
21. Less: Credit against excess profits tax (10% of item 18 (c))		$ 483 06
22. Item 20 minus item 21		$ 4,347 41
23. Amount, if any, due to application of section 734 (adjustment in case of position inconsistent with prior income tax liability) (attach schedule)		
24. Excess profits tax due (item 22 plus item 23, or item 22 minus item 23, whichever is applicable)		$ 573 38

Prorated for Fiscal Year 15/350 of $ 347.43

We, the undersigned, president (or vice president, or other principal officer) and treasurer (or assistant treasurer, or chief accounting officer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return (including any accompanying schedules and statements) has been examined by him and is, to the best of his knowledge and belief, a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Internal Revenue Code and the regulations issued thereunder.

[fol. 32]

Page 2

QUESTIONS

(a) Date of incorporation Nov. 14, 1945 (b) State or country Ky

(c) Collector's office in which your income tax return for the taxable year was filed Ky

(d) Is this a consolidated return? No If so, procure from the collector Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed as a part of the consolidated income tax return.

(e) In computing the excess profits credit under the invested capital method, do you elect to include in excess profits net income interest received on, reduced by the amount of amortizable bond premium under section 125 attributable to, all Government obligations described in section 22(b)(4) of the Internal Revenue Code? (Answer "yes" or "no") No

(f) Are you a transferor or transferee upon an exchange as defined by section 760 or 761 of the Internal Revenue Code? (Answer "yes" or "no") No

(g) Does this return involve an adjustment of the excess profits tax liability due to the application of the sections specified in (1) below? (Answer "yes" or "no") No If answer is "yes":

(1) Check the appropriate sections and submit schedules showing computation: 710(a)(4) ☐; 721 ☐; 726 ☐; 731 ☐; 735(b) ☐; 735(c) ☐; 736(a) ☐; 736(b) ☐. (See General Instructions E, F, G, H, and I.) (Enter amount of excess profits tax as Item 18 (b), page 1.

(2) From the schedules submitted under (1) above, enter any tax adjustment which results from the application of each of the following sections: 721, $; 726, $; 731, $

(3) From the schedules submitted under (1) above, enter any income adjustment which results from the application of each of the following sections: 721, $; 731, $; 735(b), $, 735(c), $

(h) State amount of total assets as of the end of the taxable year. (From Form 1120, page 4, line 8, last column.) $

(i) Has a constructive average base period net income under section 722 been used in computing the excess profits credit used on this return? If the answer is "yes," was such constructive average base period net income finally determined? Or, if not finally determined, is it used pursuant to permission granted by the Commissioner? If the answer to the first question is "yes," the following questions should be answered and the required information furnished:

(1) Is the amount of the constructive average base period net income so used the same as that which was finally determined or permitted? If the answer is "no," attach statement setting forth reasons for the variance and the amount thereof.

(2) If the constructive average base period net income resulted from the application of section 722 (b) (4) or (5) or section 722 (c), are the facts and circumstances different in the taxable year from the facts and circumstances with respect to which the claim for relief was first allowed? If so, attach statement containing a brief description of the difference and an account of its effect upon the business of the taxpayer for the taxable year.

(3) State the amount of the excess profits credit for the taxable year computed without regard to section 722. $

(j) Is any unused excess profits credit adjustment computed with the use of a constructive average base period net income? If the answer is "yes," attach schedule showing computation.

Schedule A. EXCESS PROFITS NET INCOME COMPUTATION

Line No.		Column 1 Income Credit Method		Column 2 Invested Capital Credit Method	
1.	Normal-tax net income (computed without allowance of credit for income subject to excess profits tax and without allowance of dividends received credit) (item 38, page 1, Form 1120)	$		$ 18,273	62
2.	Net short-term capital gain (do not enter net short-term capital loss)				
3.	Adjustment to net operating loss deduction				
4.	Decrease in deductions limited by income				
5.	80 percent of interest on borrowed capital	x x x x x x x	x x	39	38
6.	Interest on Government obligations (see question (e) above, for election)	x x x x x x x	x x		
7.	Total of lines 1 to 6	$		$ 18,313	00
8.	Net gain from sale or exchange of capital assets (item 12 (a) plus item 33, page 4, Form 1120)	$		$	
9.	Income from retirement or discharge of bonds, etc.				
10.	Refunds and interest on Agricultural Adjustment Act taxes				
11.	Recoveries of bad debts				
12.	Increase in deductions limited by income				
13.	(a) Dividends received credit adjustment (item 13, page 1, Form 1120, excluding dividends received from foreign corporations)			x x x x x x x	x x
	(b) Dividends received credit adjustment (item 13, page 1, Form 1120, excluding dividends received from foreign personal holding companies and dividends received on stock held primarily for sale to customers by a dealer in securities)	x x x x x x x	x x		
14.	Nontaxable income of certain industries with depletable resources				
15.	Total of lines 8 to 14	$		$	
16.	Excess profits tax net income computed without regard to deductions applicable to life insurance companies (line 7 minus line 15)	$		$	
17.	Deductions applicable to life insurance companies				
18.	Excess profits net income computed under income credit method or invested capital credit method (line 16, or line 16 minus line 17 in case of a life insurance company)	$		$ 18,313	00

16—61130-4

Page 4

Schedule C.—EXCESS PROFITS CREDIT—BASED ON INVESTED CAPITAL

Line No.			
	Equity Invested Capital at the Beginning of the Taxable Year (See instructions for Schedule C, lines 1 to 12, inclusive)		
1.	Money paid in for stock, or as paid-in surplus, or as a contribution to capital		$ -0-
2.	Property paid in for stock, or as paid-in surplus, or as a contribution to capital		-0-
3.	Distributions of earnings and profits in stock of the corporation		-0-
4.	(a) Accumulated earnings and profits	$	
	(b) Adjustment for transferor's deficit under section 718 (c) (5)	$	
	(c) Increase or decrease under section 761 (d) (1) on account of intercorporate liquidation	$	
	(d) Accumulated earnings and profits (item 4 (a)) as adjusted by item 4 (b) and (c)		-0-
5.	25 percent of new capital paid in during a taxable year beginning after December 31, 1940		-0-
6.	Increase on account of intercorporate liquidation under section 761 (d) (2)		-0-
7.	Deficit in earnings and profits of another corporation under section 718 (a) (7)		-0-
8.	Total of lines 1 to 7		$ -0-
9.	Less: Distributions made prior to the taxable year not out of accumulated earnings and profits	$	
10.	Earnings and profits of another corporation required to be deducted by section 718 (b) (3)		
11.	Decrease on account of intercorporate liquidation under section 761 (d) (2)		
12.	Deficit in earnings and profits included in invested capital of another corporation (section 718 (b) (5))		
13.	Total of lines 9 to 12		-0-
14.	Equity invested capital at beginning of taxable year (line 8 minus line 13)		$ -0-
	Average Addition to Equity Invested Capital During the Taxable Year (See instructions for Schedule C, lines 1 to 12, inclusive)		
15.	Money paid in for stock, or as paid-in surplus, or as a contribution to capital	$	
16.	Property paid in for stock, or as paid-in surplus, or as a contribution to capital		
17.	Distributions of earnings and profits (other than earnings and profits of the taxable year) in stock of the corporation (see line 24, below)		
18.	25 percent of new capital		
19.	Increase on account of intercorporate liquidation under section 761 (d) (2)		
20.	Deficit in earnings and profits of another corporation under section 718 (a) (7)		
21.	Total additions in lines 15 to 20		-0-
22.	Total of lines 14 and 21		$
	Average Reduction in Equity Invested Capital During the Taxable Year (See instructions for Schedule C, lines 1 to 12, inclusive)		
23.	Distributions not out of earnings and profits of the taxable year	$	
24.	Stock distributions from accumulated earnings and profits at beginning of year (see line 17, above)		
25.	Decrease on account of intercorporate liquidation under section 761 (d) (2)		
26.	Deficit in earnings and profits included in invested capital of another corporation (section 718 (b) (5))		
27.	Total reductions in lines 23 to 26		-0-
	(See instructions for Schedule C, lines 28 to 40, inclusive)		
28.	Average equity invested capital (line 22 minus line 27)		$
29.	Average borrowed capital (attach schedule)	$ 80,707 29	
30.	Average borrowed invested capital (50 percent of line 29)		40,353 65
31.	Average invested capital (line 28 plus line 30)		$ 40,353 65
32.	Total inadmissible assets	$	
33.	Total admissible and inadmissible assets	$	
34.	Percentage which line 32 is of line 33	%	
35.	Reduction on account of inadmissible assets (..... percent of line 31)		-0-
36.	Invested capital (line 31 minus line 35)		$ 40,353 65
37.	Portion of line 36 (not over $5,000,000); and credit at 8 percent	$	8% $ 3,228 29
38.	Portion of line 36 (over $5,000,000, but not over $10,000,000); and credit at 6 percent		6%
39.	Portion of line 36 (over $10,000,000); and credit at 5 percent		5%
40.	Excess profits credit—based on invested capital (total of lines 37 to 39)		$ 3,228 29

[fol. 34]

THE COLONY, INCORPORATED
Lexington, Kentucky
Schedules Submitted with Income Tax Return
Taxable Year Ended October 31, 1946

Schedule B - Balance Sheet as at October 31, 1946

ASSETS

Cash in Bank	863.01	
Accounts Receivable	71,631.25	
First National Bank and Trust Co. as		
Escrow Agent, Account No. 1	44,535.00	
Escrow Agent, Account No. 2	8,356.25	
Bosworth Farm - Land	72,282.88	
The Colony Subdivision	74,175.00	
Farm Buildings and Fencing	29,000.80	
Farm Equipment	670.00	
Live Stock	2,478.35	
Total Assets		303,992.54

LIABILITIES

Notes Payable - Bank Loans	149,403.00	
Notes Payable - Stockholders	57,800.00	
Accounts Payable	165.65	
Reserve for Improvements	76,074.12	
Reserve for Depreciation	706.00	
Accrued Federal Income Tax	4,589.94	
Accrued Kentucky Income Tax	570.15	
Capital Stock, 400 Shares (No Par)	1,000.00	
Surplus - Earned	13,683.68	
Total Liabilities		303,992.54

(b) Net gain (or loss) from sale or exchange of property other than capital assets (Schedule D)

13. Dividends. (From Schedule E)			
14. Other income. (State nature)			
15. Total income in items 3, and 6 to 14, inclusive	Schedule		$ 22,250 03

DEDUCTIONS

16. Compensation of officers. (From Schedule F)	$		
17. Salaries and wages (not deducted elsewhere)			
18. Rent			
19. Repairs			
20. Bad debts (From Schedule G)			
21. Interest			
22. Taxes. (From Schedule H) (Deduct declared value excess-profits tax as item 35)			
23. Contributions or gifts paid. (From Schedule I)			
24. Losses by fire, storm, shipwreck, or other casualty, or theft. (Submit schedule)			
25. Depreciation. (From Schedule J)			
26. Depletion of mines, oil and gas wells, timber, etc. (Submit schedule)			
27. Net operating loss deduction. (Submit statement)			
28. Amortization of emergency facilities. (Submit schedule)			
29. (a) Advertising			
(b) Amounts contributed under a pension, annuity, stock bonus, or profit-sharing plan, etc.			
(c) Other deductions authorized by law. (From Schedule K)			
30. Total deductions in items 16 to 29, inclusive	Schedule		$ 3,976 41
31. Net income for declared value excess-profits tax computation (item 15 minus item 30)			$ 18,273 62
32. Add: Interest on obligations of certain instrumentalities of the United States issued prior to March 1, 1941. (From Schedule M, line 15 (a) (2) (ii)) $ ... Less amortizable bond premiums, $			-0-
33. Excess of net long-term capital gain over net short-term capital loss. (From Schedule C)			-0-
34. Total of lines 31, 32, and 33			$
35. Less: Declared value excess-profits tax			-0-
36. Net income			$
37. Less: Interest on certain obligations of the United States and its instrumentalities issued prior to March 1, 1941. (Enter total of lines 9 (a) and 32)			-0-
38. Adjusted net income			$ 18,273 62
39. Less: Adjusted excess profits net income from Form 1121. (See instruction on page 9)	$		
40. Dividends received credit (85 percent of column 2, Schedule E, but not in excess of 85 percent of item 38 minus item 39, above)			
41. Normal-tax net income			$

TOTAL INCOME AND DECLARED VALUE EXCESS-PROFITS TAXES

42. Total income tax (line 28 or 30, page 2, whichever is applicable)	$	
43. Less: Credit for income taxes paid to a foreign country or United States possession allowed a domestic corporation		
44. Balance of income tax		
45. Total declared value excess-profits tax (line 8, page 2)		
46. Total income and declared value excess-profits taxes due	Fiscal year, Schedule X	$ 4,011 [illegible]

AFFIDAVIT. (See Instruction E)

We, the undersigned, president (or vice president, or other principal officer) and treasurer (or assistant treasurer, or chief accounting officer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return (including any accompanying schedules and statements) has been examined by him and is, to the best of his knowledge and belief, a true, correct, and complete return, made in good faith for the taxable year stated, pursuant to the Internal Revenue Code and the regulations issued thereunder.

Subscribed and sworn to before me this 4th day of January, 1947.

My Commission Expires December 27, 1948

NOTARIAL SEAL

Mary Louise Fagan
(Signature of officer administering oath) (Title)
Notary Public, Fayette County, Kentucky

CORPORATE SEAL

[illegible]
(Signature of Treasurer or Chief Accounting Officer)
(Print name)

AFFIDAVIT. (See Instruction E)

I/we swear (or affirm) that I/we prepared this return for the person named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the tax liability of the person for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to before me this 4 day of January, 1947

My Commission Expires December 27, 1948

NOTARIAL SEAL

Mary Louise Fagan
(Signature of officer administering oath) Notary Public, Fayette County, Kentucky

[illegible]
(Signature of person preparing this return)

[illegible] FORTUNE
(Name and address of individual preparing the return)
Corporation
(Name of firm, if any)
[illegible]
(Street and number, if any)

The Colony

(Name)

c/o Charlie Sturgill Motor Co.,

(Street and number)

Lexington, Kentucky

(City or town, postal zone number) (State)

Business group serial number entered on page 1, Form 1120

FA

Cash Check M. O.

$ 85

EXCESS PROFITS TAX COMPUTATION

	Column 1 Income Credit Method	Column 2 Invested Capital Credit Method
1. Excess profits net income (line 18, Schedule A)		$ 18,313 00
2. Specific exemption		$ 10,000 00
3. Excess profits credit—based on income (line 40, Schedule B)		xxxxxxx xx
4. Excess profits credit—based on invested capital (line 40, Schedule C)	xxxxxxx xx	8,228 29
5. Unused excess profits credit adjustment (attach schedule)		
6. Total of items 2 to 5		$ 18,228 29
7. Difference between item 1 and item 6	$	$ 5,084 71
8. Adjusted excess profits net income (item 7, column 1, or item 7, column 2, whichever is applicable)		$ 5,084 71
9. 95 percent of item 8		$ 4,830 47
10. Net income (item 36, page 1, Form 1120)		$
11. Less: (a) Dividends received credit (85 percent of total of column 2, Schedule E, Form 1120, but not in excess of 85 percent of item 10 above (excluding from the computation dividends received on certain preferred stock of a public utility))	$	
(b) Credit for dividends paid on certain preferred stocks if taxpayer is a public utility (20 percent of line 20, page 2, Form 1120)		
12. Surtax net income (computed without regard to the credit provided in section 26 (e) (sum of lines 18 and 21, page 2, Form 1120) and without regard to 80 percent of the credit provided in section 26 (h))		$
13. 80 percent of item 12		
14. Income tax under Chapter 1 (other than section 102) for the taxable year (item 42, page 1, Form 1120)		
15. Excess of item 13 over item 14		$
16. Item 9, or item 15, whichever is lesser		$
17. Amount deferred by reason of the application of section 710 (a) (5) (relating to abnormality under section 722) (attach schedule)		$
18. Excess profits tax:		
(a) Item 16 minus item 17	$	
(b) If schedule is filed under question (g), page 2, amount of tax as computed in such schedule		
(c) Item 18 (a) or item 18 (b), whichever is applicable		$
19. Less: Credit for income taxes paid to a foreign country or United States possession allowed to a domestic corporation (portion not used in computing item 43, page 1, Form 1120)		
20. Item 18 (c) minus item 19		$
21. Less: Credit against excess profits tax (10% of item 18 (c))		$ 482 95
22. Item 20 minus item 21		$ 4,347 52
23. Amount, if any, due to application of section 734 (adjustment in case of position inconsistent with prior income tax liability) (attach schedule)		
24. Excess profits tax due (item 22 plus item 23, or item 22 minus item 23, whichever is applicable)		$ 434 75

Prorated for Fiscal Year 45/350 of 4,347.52

We, the undersigned, president (or vice president, or other principal officer) and treasurer (or assistant treasurer, or chief accounting officer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return (including any accompanying schedules and statements) has been examined by him and is, to the best of his knowledge and belief, a true, correct, and complete return; made in good faith, for the taxable year stated, pursuant to the Internal Revenue Code and the regulations issued thereunder.

Subscribed and sworn to before me this 14 day of January, 194 7

My Commission Expires December 27, 1948

NOTARIAL SEAL

Mary Louise Hagan

Notary Public, Fayette County, Kentucky

(Title)

Hyde Motor Co.

(Corporate officer or other principal officer) (State title)

CORPORATE SEAL

Hyde Sturgill

(Treasurer, Assistant Treasurer, or Chief Accounting Officer) (State title)

I/we swear (or affirm) that I/we prepared this return for the person named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the excess profits tax liability of the person for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to before me this 4 day of January, 194 7

My Commission Expires December 27, 1948

NOTARIAL SEAL

Mary Louise Hagan

(Signature of person preparing this return)

PARTNER

(Address of person preparing this return)

THE COLONY, INCORPORATED
Lexington, Kentucky
Schedules Submitted with Income Tax Return
Taxable Year Ended October 31, 1946

Schedule A - Income

REVENUE

Sales of 39 lots "The Colony Subdivision"		78,987.50	
Less Cost of Lots Sold		57,375.00	
Profit on Lot Sales		21,612.50	
Sales of Farm Products		637.53	
Total Gross Revenue			22,250.03

DEDUCTIONS

Advertising			532.02	
Directors Expense			47.07	
Fertilizer			221.50	
Hauling			7.72	
Insurance			631.20	
Interest			78.75	
Salaries and Wages			853.81	
Seed and Feed			39.67	
Supplies - Farm			60.04	
Supplies - Office			130.10	
Taxes and Licenses			65.25	
Telephone and Telegraph			.83	
Gas and Oil			32.30	
Depreciation, 6 Months:				
5 Barns	23,000.00 @ 5%	575.00		
1 House	3,500.00 @ 5%	87.50		
2 Mules	100.00 @ 20%	10.00		
Farm Equipment	670.00 @ 10%	33.50	706.00	
Sub-total			3,406.26	
Accrued Kentucky Income Tax			570.15	
Total Deductions				3,976.41
Taxable Income				18,273.62
Deduct:				
Accrued Federal Income Tax				4,589.94
Surplus Addition for Year				13,683.68

THE COLONY, INCORPORATED
Lexington, Kentucky
Schedules Submitted with Income Tax Return
Taxable Year Ended October 31, 1946

Schedule I, Computation of Normal and Surtax for Fiscal Year

Tax Computed at 1945 Rates:						
Net Income, Line 38, Form 1120					18,273.62	
Less Excess Profits Income, Line 8, Form 1121					5,084.71	
Subject to Normal and Surtax					13,188.91	
Normal tax on	5,000.00	@	15%	750.00		
Do	8,188.91	@	17%	1,392.11	2,142.11	
Surtax on	13,188.91	@	10%		1,318.89	
Total at 1945 Rates					3,461.00	
Pro-rated 46/350ths						454.87
Tax Computed at 1946 Rates:						
Net Income, Line 38, Form 1120					18,273.62	
Normal tax on	5,000.00	@	15%	750.00		
Do	13,273.62	@	17%	2,256.52	3,006.52	
Surtax on	18,273.62	@	6%		1,096.41	
Total at 1946 Rates					4,102.93	
Pro-rated 304/350ths						3,563.69
Total Normal Tax and Surtax						4,018.56

[fol. 36]

Schedule E.—INCOME FROM DIVIDENDS

Page

1. Name and Address of Payer Corporation	2. Domestic Corporations Taxable Under Chapter 1, Internal Revenue Code	3. Foreign Corporations	4. Other Corporations
	$	$	$
Totals	$	$	$
Total of columns 2, 3, and 4. (Enter as item 13, page 1)			$

*Except dividends received from corporations organized under the China Trade Act, 1922, and corporations entitled to the benefits of section 251 of the Internal Revenue Code, which dividends should be entered in column 4.

Dividends on share accounts in Federal savings and loan associations in case of share accounts issued prior to March 28, 1942, should not be listed, but the amount should be included in items 28 and 37, page 1; dividends on share accounts issued on or after March 28, 1942, should be reported in column 4.

Schedule F.—COMPENSATION OF OFFICERS

1. Name and Address of Officer	2. Official Title	3. Time Devoted to Business	Percentage of Corporation's Stock Owned		6. Amount of Compensation
			4. Common	5. Preferred	
					$
Total compensation of officers. (Enter as item 16, page 1)					$

NOTE.—Schedule F-1 (IN DUPLICATE) also must be filed with this return if compensation in excess of $75,000 was paid to any officer or employee.

Schedule G.—BAD DEBTS. (See Instruction 20) (See notes 1 and 2)

1. Taxable Year	2. Net Income Reported	3. Sales on Account	4. Bad Debts of Corporation If No Reserve Is Carried on Books (See note 2)	If Corporation Carries a Reserve—	
				5. Gross Amount Added to Reserve	6. Amount Charged Against Reserve
1941	$	$	$	$	$
1942					
1943					
1944					
1945					

1. Check whether deduction claimed represents debts which have become worthless ☐, or is an addition to a reserve ☐.
2. Not including securities which are capital assets and which became worthless within the taxable year. Such securities which became worthless within the year should be reported in Schedule C.

Schedule H.—TAXES. (See Instruction 22)

Nature	Amount
	$
Total. (Enter as item 22, page 1)	$

Schedule I.—CONTRIBUTIONS OR GIFTS PAID. (See Instruction 23)

Name and Address of Organization	Amount
	$
Total. (Enter as item 23, page 1, subject to 5 percent limitation.) (See Instruction 23)	$

Schedule J.—DEPRECIATION. (See Instruction 25)

1. Kind of Property (If buildings, state material of which constructed)	2. Date Acquired	3. Cost or Other Basis (Do not include land or other nondepreciable property)	4. Assets Fully Depreciated in Use at End of Year	5. Depreciation Allowed (or allowable) in Prior Years	6. Remaining Cost or Other Basis To Be Recovered	7. Estimated Life Used in Accumulating Depreciation	8. Estimated Remaining Life From Beginning of Year	9. Depreciation Allowable This Year
		$	$	$	$			$
Total. (Enter as item 25, page 1)								$

Schedule K.—OTHER DEDUCTIONS. (See Instruction 29)

QUESTIONS

1. Date incorporated Nov. 14-1945 2. State or country Ky.
3. If incorporated in 1945, indicate whether (a) completely new business ☐, or (b) successor to previously existing business, which was organized as (1) corporation ☐, (2) partnership ☐, or (3) sole proprietorship ☐, or (4) other (indicate) ..... If successor to previously existing business, give name and address of the previous business organization .....
4. Collector's office where the corporation's return for the preceding year was filed .....
5. Enter amount of income (or deficit) from Item 34, page 1, Form 1120 for 1944 .....
6. The corporation's books are in care of Charles Bingell
Located at Lexington, Ky.
7. Enter the approximate number of stockholders at the close of the taxable year 1
8. Did the corporation during the taxable year have any Government contracts or subcontracts? (Answer "yes" or "no") No If answer is "yes," state the approximate aggregate gross dollar amount billed during the taxable year under all such contracts and/or subcontracts. (See Instruction G-(3).) $.....
9. Is the corporation a personal holding company within the meaning of section 501 of the Internal Revenue Code? No (If so, an additional return on Form 1120 H must be filed.)
10. Is this a consolidated return? No (If so, procure from the collector of internal revenue for your district Form 851, Affiliations Schedule, which shall be filled in, sworn to, and filed as a part of this return.)
11. If this is not a consolidated return: (a) did the corporation own at any time during the taxable year 50 percent or more of the voting stock of another corporation either domestic or foreign? No; or (b) did any corporation, individual, partnership, trust, or association own at any time during the taxable year 50 percent or more of the corporation's voting stock? ..... (If either answer is "yes," attach separate schedule showing: (1) Name and address; (2) percentage of stock owned; (3) date stock was acquired; and (4) the collector's office in which the income tax return of such corporation, individual, partnership, trust, or association for the last taxable year was filed.)
12. Is this return made on the basis of cash receipts and disbursements? No If not, describe fully in separate statement Accruals
13. Has the corporation in this return taken a deduction for any amount of wages or salaries representing an increase or decrease in rate? (Answer "yes" or "no") No If so, attach statement as required by Instructions 16 and 17.
14. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower ..... If other basis is used, explain fully in separate statement, giving date inventory was last reconciled with stock.
15. Did the corporation make a return of information on Forms 1096 and 1099 or Form W-2a for the calendar year 1945 (see Instruction G-(1))? No
16. Has any transaction described in Instruction G-(6) occurred on or after October 8, 1940? (Answer "yes" or "no") No
17. Did the corporation at any time during the taxable year own directly or indirectly any stock of a foreign corporation? No (If so, submit statement as required by Instruction K-(2).)

Schedule L.—BALANCE SHEETS. (See Instruction I.)

ASSETS	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
1. Cash		$		$
2. Notes and accounts receivable	$		$	
Less: Reserve for bad debts				
3. Inventories (itemize in separate schedule)				
4. Investments in governmental obligations:				
(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	$		$	
(b) Obligations of the United States				
(1) Obligations issued on or before September 1, 1917; all postal savings bonds; Treasury notes issued prior to December 1, 1940, and Treasury bills issued prior to March 1, 1941				
(2) United States savings bonds and Treasury bonds issued prior to March 1, 1941				
(3) Treasury notes issued on or after December 1, 1940, and all other obligations of the United States issued on or after March 1, 1941				
(c) Obligations of instrumentalities of the United States				
(1) Obligations of Federal land banks, joint stock land banks, and Federal intermediate credit banks issued prior to March 1, 1941				
(2) Obligations issued by other instrumentalities of the United States prior to March 1, 1941				
(3) Obligations of all instrumentalities of the United States issued on or after March 1, 1941				
5. Other investments (itemize)				
6. Capital assets:				
(a) Depreciable assets (itemize in separate schedule)	$		$	
Less: Reserve for depreciation				
(b) Depletable assets	$		$	
Less: Reserve for depletion				
(c) Land				
7. Other assets (itemize)	$		$	
8. TOTAL ASSETS		$		$
LIABILITIES				
9. Accounts payable		$		$
10. Bonds, notes, and mortgages payable:				
(a) With original maturity of less than 1 year	$		$	
(b) With original maturity of 1 year or more				
11. Accrued expenses (itemize)	$		$	
12. Other liabilities (itemize)	$		$	
13. Surplus reserves (itemize in separate schedule)				
14. Capital stock: Number of shares at end of year—				
(a) Preferred stock ( )	$		$	
(b) Common stock ( )				
15. Paid-in or capital surplus				
16. Earned surplus and undivided profits				
17. TOTAL LIABILITIES		$		$

SCHEDULE B

Schedule M.—RECONCILIATION OF NET INCOME AND ANALYSIS OF EARNED SURPLUS AND UNDIVIDED PROFITS

1. Total distributions to stockholders charged to earned surplus during the taxable year:			13. Earned surplus and undivided profits at close of preceding taxable year (Schedule L)	$
(a) Cash	$		14. Adjusted net income (item 38, page 1)	
(b) Stock of the corporation			15. Nontaxable and partially exempt income:	
(c) Other property			(a) Interest on:	
2. Contributions (excess over 5 percent limitation)			(1) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	
3. Federal income and excess-profits taxes			(2) Obligations of the United States:	
4. Income taxes claimed as a credit in whole or in part in item 43, page 1			(i) Obligations issued on or before September 1, 1917; all postal savings bonds; Treasury notes issued prior to December 1, 1940; and Treasury bills issued prior to March 1, 1941	
5. Federal taxes paid on tax-free covenant bonds				
6. Excess of capital losses over capital gains				

[fol. 38]

35

17. TOTAL LIABILITIES ... | | $ | $

Schedule M.—RECONCILIATION OF NET INCOME AND ANALYSIS OF EARNED SURPLUS AND UNDIVIDED PROFITS

1. Total distributions to stockholders charged to earned surplus during the taxable year:		
(a) Cash	$	
(b) Stock of the corporation		
(c) Other property		
2. Contributions (excess over 5 percent limitation)		
3. Federal income and excess-profits taxes		
4. Income taxes claimed as a credit in whole or in part in item 43, page 1		
5. Federal taxes paid on tax-free covenant bonds		
6. Excess of capital losses over capital gains		
7. Additions to surplus reserves (list separately):		
(a)		
(b)		
8. Other unallowable deductions:		
(a)		
(b)		
9. Adjustments not recorded on books (itemize):		
(a)		
(b)		
10. Sundry debits to earned surplus (itemize):		
(a)		
(b)		
11. Earned surplus and undivided profits at close of the taxable year (Schedule L)		
12. Total of lines 1 to 11	$	

SCHEDULE A

13. Earned surplus and undivided profits at close of preceding taxable year (Schedule L)	$	
14. Adjusted net income (item 38, page 1)		
15. Nontaxable and partially exempt income:		
(a) Interest on:		
(1) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia; or United States possessions		
(2) Obligations of the United States:		
(i) Obligations issued on or before September 1, 1917; all postal savings bonds; Treasury notes issued prior to December 1, 1940; and Treasury bills issued prior to March 1, 1941		
(ii) United States savings bonds and Treasury bonds owned in the principal amount of $5,000 or less, issued prior to March 1, 1941		
(iii) United States savings bonds and Treasury bonds owned in excess of the principal amount of $5,000 issued prior to March 1, 1941		
(3) Obligations of instrumentalities of the United States:		
(i) Obligations of Federal land banks, joint stock land banks, and Federal intermediate credit banks issued prior to March 1, 1941		
(ii) Obligations issued by other instrumentalities of the United States prior to March 1, 1941		
(b) Other nontaxable income (itemize):		
(1)		
(2)		
16. Charges against surplus reserves (itemize):		
17. Adjustments not recorded on books (itemize):		
18. Sundry credits to earned surplus (itemize):		
19. Total of lines 13 to 18	$	

EXCESS PROFITS TAX. (See Instructions for Form 1121)

(a) Is an excess profits tax return on Form 1121 being filed for the taxable period covered by this return? ... Yes

(b) If a personal service corporation (other than a member of an affiliated group of corporations filing a consolidated return) signifies below its desire not to be subject to the excess profits tax, it shall be exempt from such tax and the provisions of Supplement S, Chapter 1, shall apply to the shareholders in such corporation who were such shareholders on the last day of the taxable year of the corporation. (Attach Form 1121PS)

(c) If corporation claims exemption under section 727 of the Internal Revenue Code, state basis of claim ...

(d) If an excess profits tax return is not being filed for the reason that it is claimed that the excess profits net income computed under the invested capital method is not greater than (1) $10,000 for a taxable year ending in 1945, or (2) an amount equal to the sum of the portion of $10,000 applicable to the part of the year falling in 1945 and the portion of $25,000 applicable to the part of the year falling in 1946, in case of a taxable year beginning in 1945 and ending in 1946, the following Schedule N should be filled in. The completion of Schedule N does not constitute the filing of an excess profits tax return.

Schedule N.—EXCESS PROFITS NET INCOME COMPUTATION

1. Normal-tax net income (computed without credit for income subject to excess profits tax and dividends received credit) (item 28, page 1)	$	
2. Net short-term capital gain (do not enter net short-term capital loss)		
3. 30 percent of interest on borrowed capital		
4. Adjustment to net operating loss deduction under section 711 (a) (2) (L)		
5. Total of lines 1 to 4	$	
6. Dividends received credit adjustment (item 13, page 1, excluding the sum of (a) dividends received (actual or constructive) from foreign personal holding companies, and (b) dividends received on stock held primarily for sale to customers by a dealer in securities)		$
7. Net gain from sale or exchange of capital assets (item 12 (a), plus item 23, page 1)		
8. Income from retirement or discharge of bonds, etc.		
9. Refunds and interest on Agricultural Adjustment Act taxes		
10. Recoveries of bad debts		
11. Total of lines 6 to 10		$

12. Excess profits net income (for purpose of determining necessity for filing return) (line 5 minus line 11) ... $

16—41120-8

Computation proved

Form 1120 Treasury Department Internal Revenue Service

Fiscal Year

UNITED STATES
CORPORATION INCOME TAX RETURN

For Calendar Year 1946

or fiscal year beginning Nov. 1, 1946, and ending Oct. 31, 1947

3) 1946

FILED DEC 24 1947

Serial No. 4[illegible]

District Kentucky

PAID 17. DEC 24 1947

Collector's Office District of Kentucky Cash Check M. O.

First Payment $

[fol. 39]

2.76

PRINT PLAINLY CORPORATION'S NAME AND ADDRESS

The Colony, Inc. (Name)

145 East High St (Street and number)

Lexington (City or town, postal zone number) Ky (State)

Kind of business: Farm - Real Estate

Business group serial number (from Instruction N)

Number of places of business

NORMAL-TAX NET INCOME COMPUTATION

GROSS INCOME

1.	Gross sales (where inventories are an income-determining factor) $; Less: Returns and allowances $		
2.	Cost of goods sold. (From Schedule A)		
3.	Gross profit from sales		
4.	Gross receipts (where inventories are not an income-determining factor) $; Less: Cost of operations (From Schedule B)		
5.	By: J. R. Thompson		
6.	Gross profit, where inventories are not an income-determining factor		
7.	Interest on loans, notes, mortgages, bonds, bank deposits, etc		
8.	Interest on corporation bonds, etc $		
9.	(a) Interest on United States savings bonds and Treasury bonds owned in excess of the principal amount of $5,000 issued prior to March 1, 1941. (From Schedule M, line 19 (a) (2) (iii))		
	(b) Interest on obligations of certain instrumentalities of the United States issued prior to March 1, 1941. (From Schedule M, line 19 (a) (3) (ii))		
	(c) Interest on Treasury notes issued on or after December 1, 1940, and obligations issued on or after March 1, 1941, by the United States or any agency or instrumentality thereof. (Submit schedule)		
10.	Rents		
11.	Royalties		
12.	(a) Excess of net short-term capital gain over net long-term capital loss. (From Schedule C)		
	(b) Excess of net long-term capital gain over net short-term capital loss. (From Schedule C)		
	(c) Net gain (or loss) from sale or exchange of property other than capital assets. (From Schedule D)		
13.	Dividends. (From Schedule E)		
14.	Other income. (State nature)		
15.	Total income in items 3, and 6 to 14, inclusive. Schedule A		$ 18,095 41

THE TAX COURT OF THE U.S. DIV. 13 DOCKET 5368 ACQUIESCED IN OCT 26 1955 E

Rec'd with Return DEC 23 1947 61 Coll. Int. Rev. Dist. of Ky.

P 3/4/49 R.A.R. ATT'D TO

DEDUCTIONS

16.	Compensation of officers. (From Schedule F)	$	
17.	Salaries and wages (not deducted elsewhere)		
18.	Rent		
19.	Repairs		
20.	Bad debts. (From Schedule G)		
21.	Interest		
22.	Taxes. (From Schedule H)		
23.	Contributions or gifts paid. (From Schedule I)		
24.	Losses by fire, storm, shipwreck, or other casualty, or theft. (Submit schedule)		
25.	Depreciation. (From Schedule J)		
26.	Depletion of mines, oil and gas wells, timber, etc. (Submit schedule)		
27.	Net operating loss deduction. (Submit statement)		
28.	Amortization of emergency facilities. (Submit schedule)		
29.	(a) Advertising		
	(b) Amounts contributed under a pension, annuity, stock bonus, or profit-sharing plan, etc		
	(c) Other deductions authorized by law. (From Schedule K)		
30.	Total deductions in items 16 to 29, inclusive. Schedule A		18,053 38
31.	Net income (item 15 minus item 30)		$ 41 73
32.	Less: Interest on certain obligations of the United States and its instrumentalities issued prior to March 1, 1941. (Enter total of items 9 (a) and (b))		-0-
33.	Adjusted net income		$
34.	Less: Dividends received credit (85 percent of column 2, Schedule E, but not in excess of 85 percent of item 33, above)		-0-
35.	Normal-tax net income		$ 41 73

TOTAL INCOME TAX

36.	Total income tax (line 19, page 3)	$ 8 76	
37.	Less: Credit for income taxes paid to a foreign country or United States possession allowed a domestic corporation		
38.	Balance of income tax due		$ 8 76

AFFIDAVIT. (See Instruction E)

We, the undersigned, president (or vice president, or other principal officer) and treasurer (or assistant treasurer, or chief accounting officer) of the corporation for which this return is made, being severally duly sworn, each for himself deposes and says that this return (including any accompanying schedules and statements) has been examined by him and is, to the best of his knowledge and belief, a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Internal Revenue Code and the regulations issued thereunder.

Subscribed and sworn to before me this 17th day of December, 1947

Hugh Mennitten President (Signature of officer (or other principal officer)) (Official title)

MY COMMISSION EXPIRES JUNE 4, 1950

NOTARIAL SEAL

Ann Lewin Swift Notary Public (Signature of officer administering oath) (Title)

CORPORATE SEAL

F. Hoge Jr. Treas. (Treasurer, Assistant Treasurer, or Chief Accounting Officer) (Official title)

AFFIDAVIT. (See Instruction E)

I/we swear (or affirm) that I/we prepared this return for the person named herein and that the return (including any accompanying schedules and statements) is a true, correct, and complete statement of all the information respecting the tax liability of the person for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to before me this 15 day of December, 1947

NOTARIAL SEAL

My Commission Expires [illegible] 1950

(Signature of officer administering oath) (Title)

Notary Public, Fayette County Ky.

(Signature of person preparing this return)

(Name of firm or employer, if any)

HIPNER AND FORTUNE

Certified Public Accountants

(Street and number, city or town, and State)

THE COLONY, INCORPORATED
Lexington, Kentucky
Schedules Submitted with Income Tax Return
Taxable Year Ended October 31, 1947

Schedule B - Balance Sheets as at

	October 31 1946	October 31 1947
ASSETS		
Cash in Bank	863.01	1,279.28
Accounts Receivable	71,631.25	42,535.21
Notes Receivable	-0-	13,487.46
First National Bank and Trust Co. Escrow Agent	52,891.25	21,076.29
Bosworth Farm - Land	72,282.88	72,282.88
The Colony Subdivision - Lots	74,175.00	55,600.00
Farm Buildings and Fencing	29,000.80	29,000.80
Farm Equipment	670.00	1,163.25
Live Stock	2,478.35	2,441.09
Total Assets	303,992.54	238,865.24
LIABILITIES		
Notes Payable - Bank Loans	149,403.00	122,767.58
Notes Payable - Stockholders	57,800.00	57,800.00
Accounts Payable	165.65	-0-
Reserve for Improvements	76,074.12	40,323.42
Reserve for Depreciation —	706.00	2,267.86
Accrued Federal Income Tax	4,589.84	8.76
Accrued Kentucky Income Tax	570.15	1.67
Accrued State and County Taxes	-0-	990.00
Surplus - Earned	13,683.68	13,685.37
Capital Stock, 400 Shares (No Par)	1,000.00	1,000.00
Total Liabilities	303,992.54	238,865.24

[illegible]

[illegible]

Farm Sales

Hogs		488.35
Cattle		4,901.13
Sheep, Lambs, Wool		502.85
Tobacco		8,737.33
Barley		1,203.92
Hay		297.83
Total		14,049.35
Less:		
Cost of Cattle Sold	3,840.65	
Cost of Sheep Sold	486.00	
1/8 of Tobacco to Bosworth Estate	1,127.89	5,454.54
Gross Profit - Farm		8,595.41
Sales of 9 Lots	28,075.00	
Less Cost of Lots Sold	19,575.00	
Gross Profits - Lots		9,500.00
Total Gross Revenue		18,095.41

DEDUCTIONS

Depreciation	1,561.86	
Taxes	1,934.65	
Interest	9,032.67	
Repairs	774.57	
Expenses General	5,049.93	
Total Deductions		18,053.68
Taxable Income		41.73
Deduct:		
Ky. Department of Revenue, Penalty	29.01	
Accrued Federal Income Tax	8.76	
Accrued Ky. Income Tax	1.67	39.44
Surplus Addition for Year		2.29
Add:		
Surplus Nov. 1, 1946		13,683.68
Surplus October 31, 1947		13,685.97

THE COLONY, INCORPORATED
Lexington, Kentucky
Schedules Submitted with Income Tax Return
Taxable Year Ended October 31, 1947

Schedule A-1 - Depreciation

Property	Cost	Rate	Depreciation Sustained Current	Prior	Total
5 Barns - 4-27-1946	23,000.00	5%	1,150.00	575.00	1,725.00
1 House "	3,500.00	5%	175.00	87.50	262.50
Re-habilitation above 1946	2,500.00	5%	125.00	-0-	125.00
2 Mules 5-16-1946	100.00	20%	20.00	10.00	30.00
Farm Equipment 1946	670.00	10%	67.00	33.50	100.50
Tractor Mower 7-23-1947 (1/4)	493.25	20%	24.66	-0-	24.66
Tools " (1/4)	8.25	10%	.20	-0-	.20
Totals			1,561.86	706.00	2,267.86

Schedule A-2 - Taxes

Stamps on Deeds	73.00
Ky. Corporation License	79.66
Bank Deposits	44.59
Sheriff, Fayette County	1,437.40
Total	1,634.65

Schedule A-3 - Interest

Ky. Dept. of Revenue	6.77
First National Bank & Trust Co.	9,025.86
Adjustment, Leet Notes	.04
Total	9,032.67

Schedule A-4 - Repairs

Repairs - Buildings	547.63
Repairs - Equipment	226.94
Total	774.57

Schedule A-5 - Expenses General

Advertising	230.60
Directors Expense	42.40
Fertilizer	6.00
Coke	205.05
Insurance	528.68
Salaries - Farm	794.72
Salaries - Clerical	431.80
Seed and Feed	878.22
Supplies and Expense - Farm	141.82
Do - Office	260.64
Telephone and Telegraph	6.76
Legal and Accounting	1,012.50
Gas and Oil	109.10
Miscellaneous Farm Expense	401.54
Total	5,049.93

INCOME TAX COMPUTATION. (See Tax Computation Instructions)

Line No.	NORMAL TAX COMPUTATION	Column 1	Col. 2 Rate	Column 3 Amount of Tax
	DOMESTIC CORPORATIONS WITH NORMAL-TAX NET INCOMES NOT OVER $50,000			
1.	Normal-tax net income (item 35, page 1)	$ 41 73		
2.	Portion of line 1 (not in excess of $5,000); and tax at 15 percent	$ 41 73	15%	$ 6 26
3.	Portion of line 1 (in excess of $5,000 and not in excess of $20,000); and tax at 17 percent		17%	
4.	Portion of line 1 (in excess of $20,000 and not in excess of $25,000); and tax at 19 percent		19%	
5.	Portion of line 1 (in excess of $25,000); and tax at 31 percent		31%	
6.	Total normal tax (total tax in column 3 of lines 2, 3, 4, and 5)			$ 6 26
	DOMESTIC CORPORATIONS WITH NORMAL-TAX NET INCOMES OF OVER $50,000 AND FOREIGN CORPORATIONS ENGAGED IN BUSINESS WITHIN THE UNITED STATES IRRESPECTIVE OF AMOUNT OF NORMAL-TAX NET INCOME			
7.	Normal-tax net income (item 35, page 1)	$		
8.	Normal tax (24 percent of line 7)		24%	$
	SURTAX COMPUTATION			
9.	Net income (item 31, page 1)	$		
10.	Less: Dividends received credit (85 percent of column 2, Schedule E, but not in excess of 85 percent of item 33, page 1 (excluding from the computation certain dividends received on preferred stock of a public utility))	$		
11.	Dividends paid on certain preferred stock if taxpayer is a public utility			
12.	Surtax net income	$		
	CORPORATIONS WITH SURTAX NET INCOMES NOT OVER $50,000			
13.	Portion of line 12 (not in excess of $25,000); and tax at 6 percent (or 8 percent in the case of a consolidated return)	$ 41 73	6%	$ 2 50
14.	Portion of line 12 (in excess of $25,000 and not in excess of $50,000); and tax at 22 percent (or 24 percent in the case of a consolidated return)		22%	
15.	Total surtax in column 3 of lines 13 and 14			$ 2 50
	CORPORATIONS WITH SURTAX NET INCOMES OF OVER $50,000			
16.	Surtax net income (line 12 above)	$		
17.	Surtax (14 percent of line 16) (or 16 percent in the case of a consolidated return)		14%	$
18.	Total normal tax and surtax (line 6 or 8, plus line 15 or 17, whichever is applicable)			$ 8 76
19.	Total tax (line 18, or line 20 of Schedule C)			$

QUESTIONS

1. Date incorporated 1945

2. State or country Ky.

3. If incorporated in 1946, indicate whether (a) completely new business ☐, or (b) successor to previously existing business, which was organized as (1) corporation ☐, (2) partnership ☐, or (3) sole proprietorship ☐, or (4) other (indicate) . If successor to previously existing business, give name and address of the previous business organization

4. Collector's office where the corporation's return for the preceding year was filed Ky.

5. Enter amount of income (or deficit) from Item 34, page 1, Form 1120 for 1945 $

6. The corporation's books are in care of J. E. Marks

Located at Lexington, Ky.

7. Enter the approximate number of stockholders at the close of the taxable year 6

8. If the total of Line 1 of Schedule M, page 4, is less than 70% of the earnings and profits for the taxable year, state reasons for retention of such earnings and profits. (See Instruction J)

9. Indicate whether the corporation is a farmers' marketing or purchasing cooperative association ☐, or a consumers' cooperative association ☐

10. Is the corporation a personal holding company within the meaning of section 501 of the Internal Revenue Code? No (If so, an additional return on Form 1120 H must be filed.)

11. Is this a consolidated return? No (If so, procure from the collector of internal revenue for your district Form 851, Affiliations Schedule, which shall be filed in, sworn to, and filed as a part of this return.)

12. If this is not a consolidated return: (a) Did the corporation own at any time during the taxable year 50 percent or more of the voting stock of another corporation either domestic or foreign? No; or (b) did any corporation, individual, partnership, trust, or association own at any time during the taxable year 50 percent or more of the corporation's voting stock? No (If either answer is "yes," attach separate schedule showing: (1) Name and address; (2) percentage of stock owned; (3) date stock was acquired; and (4) the collector's office in which the income tax return of such corporation, individual, partnership, trust, or association for the last taxable year was filed.)

13. Is this return made on the basis of cash receipts and disbursements? No If not, describe fully in separate statement. Accrual

14. Has the corporation in this return taken a deduction for any amount of wages or salaries representing an increase or decrease in rates *which required approval* in order to be deemed lawful under the Act of October 2, 1942, as amended, and regulations issued thereunder, or the establishment of rates in new plants or new departments requiring such approval? (Answer "yes" or "no") No If so, attach statement as required by Instructions 16 and 17.

15. State whether the inventories at the beginning and end of the taxable year were valued at cost, or cost or market, whichever is lower None If other basis is used, explain fully in separate statement, giving date inventory was last reconciled with stock.

16. Did the corporation make a return of information on Forms 1096 and 1099 or Form W-2a for the calendar year 1946 (see Instruction G-(1))? No

17. Has any transaction described in Instruction G-(3) occurred on or after October 8, 1940? (Answer "yes" or "no") No

18. Did the corporation at any time during the taxable year own directly or indirectly any stock of a foreign corporation? No (If so, attach statement as required by Instruction K-(3).)

16—69361-1

Schedule L.—BALANCE SHEETS. (See Instruction L)

ASSETS	Beginning of Taxable Year: Amount	Beginning of Taxable Year: Total	End of Taxable Year: Amount	End of Taxable Year: Total
1. Cash		$		$
2. Notes and accounts receivable	$		$	
Less: Reserve for bad debts				
3. Inventories:				
(a) Raw materials	$		$	
(b) Work in process				
(c) Finished goods				
(d) Supplies				
4. Investments in governmental obligations:				
(a) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	$		$	
(b) Obligations of the United States:				
(1) Obligations issued on or before September 1, 1917; all postal savings bonds; Treasury notes issued prior to December 1, 1940; and Treasury bills issued prior to March 1, 1941				
(2) United States savings bonds and Treasury bonds issued prior to March 1, 1941				
(3) Treasury notes issued on or after December 1, 1940, and all other obligations of the United States issued on or after March 1, 1941				
(c) Obligations of instrumentalities of the United States				
(1) Obligations of Federal land banks, joint stock land banks, and Federal intermediate credit banks issued prior to March 1, 1941				
(2) Obligations issued by other instrumentalities of the United States prior to March 1, 1941				
(3) Obligations of all instrumentalities of the United States issued on or after March 1, 1941				
5. Other investments (itemize)	$		$	
6. Capital assets:				
(a) Depreciable assets (itemize)	$		$	
Total depreciable assets	$		$	
Less: Reserve for depreciation				
(b) Depletable assets	$		$	
Less: Reserve for depletion				
(c) Land				
7. Other assets (itemize)	$		$	
8. TOTAL ASSETS		$		$
LIABILITIES				
9. Accounts payable		$		$
10. Bonds, notes, and mortgages payable:				
(a) With original maturity of less than 1 year	$		$	
(b) With original maturity of 1 year or more				
11. Accrued expenses (itemize)	$		$	
12. Other liabilities (itemize)	$		$	
13. Surplus reserves (itemize)	$		$	
14. Capital stock: Number of shares at end of year—				
(a) Preferred stock ..... ( )	$		$	
(b) Common stock ..... ( )				
15. Paid-in or capital surplus				
16. Earned surplus and undivided profits				
17. TOTAL LIABILITIES		$		$

Schedule M.—RECONCILIATION OF NET INCOME AND ANALYSIS OF EARNED SURPLUS AND UNDIVIDED PROFITS

1. Total distributions to stockholders charged to earned surplus during the taxable year:		17. Earned surplus and undivided profits at close of preceding taxable year (Schedule L)	$
(a) Cash	$	18. Adjusted net income (item 33, page 1)	
(b) Stock of the corporation		19. Nontaxable and partially exempt income:	
(c) Other property		(a) Interest on:	
2. Contributions or gifts (excess over 5 percent limitation)		(1) Obligations of a State, Territory, or political subdivision thereof, or the District of Columbia, or United States possessions	
3. Federal income and excess profits taxes		(2) Obligations of the United States:	
4. Income taxes of foreign countries or United States possessions if claimed as a credit in whole or in part in item 37, page 1		(i) Obligations issued on or before September 1, 1917; all postal savings bonds, Treasury notes issued prior to December 1, 1940, and Treasury bills issued prior to March 1, 1941	
5. Federal taxes paid on tax-free covenant bonds		(ii) United States savings bonds and Treasury bonds owned in the principal amount of $5,000 or less, issued prior to March 1, 1941	
6. Special improvement taxes tending to increase the value of the property assessed		(iii) United States savings bonds and Treasury bonds owned in excess of the principal amount of $5,000 issued prior to March 1, 1941	
7. Replacements, renewals, and capital expenditures charged to expenses on the books		(3) Obligations of instrumentalities of the United States:	
8. Insurance premiums paid on the life of any officer or employee where the corporation is directly or indirectly a beneficiary		(i) Obligations of Federal land banks, joint stock land banks, and Federal intermediate credit banks issued prior to March 1, 1941	
9. Unallowable interest incurred in purchasing or carrying exempt interest obligations		(ii) Obligations issued by other instrumentalities of the United States prior to March 1, 1941	
10. Excess of capital losses over capital gains		(b) Other nontaxable income (itemize)	
11. Additions to surplus reserves (list separately):		(1)	
(a)		(2)	
(b)		20. Charges against surplus reserves deducted from income in the return (itemize):	
(c)		(a)	
(d)		(b)	
12. Other unallowable deductions:		21. Adjustments for tax purposes not recorded on books (itemize):	
(a)		(a) Schedule A	
(b)		(b)	
13. Adjustments for tax purposes not recorded on books (itemize):		22. Sundry credits to earned surplus (itemize):	
(a)		(a)	
(b)		(b)	
14. Sundry debits to earned surplus (itemize):		(c)	
(a)		23. Total of lines 17 to 22	$
(b)			
(c)			
15. Earned surplus and undivided profits as shown by balance sheet at close of the taxable year (Schedule L)			
16. Total of lines 1 to 15	$		

[fol. 44]

41

16—62681-1 ★ U. S. GOVERNMENT PRINTING OFFICE

[fol. 46] MINUTE ENTRY OF ARGUMENT AND SUBMISSION—April 10, 1957 (omitted in printing).

IN UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

JUDGMENT—Filed April 22, 1957

The sole question on this review is whether the five-year statute of limitations contained in section 275(c) of the Internal Revenue Code of 1939 was applicable in this case, as the Tax Court held.[1]

The petitioner is a corporation dealing in real estate. Its income tax returns for the years in question contained understatements of gross income of more than twenty-five per cent resulting from an erroneous overstatement of the [fol. 47] basis of land sold, rather than from any omission of gross receipts. Under these circumstances it is the petitioner's contention that the general three-year limitation period of section 275 (a) of the 1939 Code is applicable. As petitioner's counsel correctly points out, the decisions of the Courts of Appeals of several other circuits give clear support to this view. *Uptegrove Lumber Co.* v. *Commissioner*, 204 F. (2d) 570 (3 Cir., 1953); *Deakman-Wells Co.* v. *Commissioner*, 213 F. (2d) 894 (3 Cir., 1954); *Goodenow* v. *Commissioner*, 238 F. (2d) 20 (8 Cir., 1956); cf. *Slaff* v. *Commissioner*, 220 F. (2d) 65 (9 Cir., 1955); *Davis* v. *Hightower*, 230 F. (2d) 549 (5 Cir., 1956).

The reasoning of these cases is not without considerable persuasive force, and if the question were here for the first time, we might be disposed to follow them. However, the question has already been decided by this court in *Reis* v. *Commissioner*, 142 F. (2d) 900 (6 Cir., 1944), where it was held that the five-year limitation was applicable when the taxpayer's understatement of gross income of more than twenty-five per cent was the result of his overstatement of

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[1] "(c) Omission from gross income. If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed."

the cost basis of property sold. The facts in the *Reis* case are, of course, not identical with the facts in the present case, but the issue presented is the same.

Upon the authority of *Reis* v. *Commissioner* the decision of the Tax Court is affirmed.

[fol. 48] Clerk's Certificate (omitted in printing).

[fol. 49] SUPREME COURT OF THE UNITED STATES
No. 306, October Term, 1957

THE COLONY, INC., Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE

ORDER ALLOWING CERTIORARI—October 14, 1957

The petition herein for a writ of certiorari to the United States Court of Appeals for the Sixth Circuit is granted, and the case is transferred to the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Whittaker took no part in the consideration or decision of this application.